

2005

Comprehensive Annual Financial Report

For the fiscal year ended
June 30, 2005



State of Arizona
Department of Transportation

Arizona Department of Transportation
Comprehensive Annual Financial Report
For the Fiscal Year Ended June 30, 2005

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INTRODUCTORY SECTION



Arizona Department of Transportation

Office of the Director

206 South Seventeenth Avenue Phoenix, Arizona 85007-3213

Janet Napolitano
Governor

Victor M. Mendez
Director

October 31, 2005

David P. Jankofsky
Deputy Director

The Honorable Janet Napolitano,
Governor of the State of Arizona,
Members of the Legislature, and
Citizens of the State of Arizona

The Arizona Department of Transportation (Department) is pleased to submit the Comprehensive Annual Financial Report (CAFR) of the Department for the fiscal year ended June 30, 2005. The CAFR is presented in three sections: Introductory, Financial, and Statistical. The **Introductory Section** includes this letter of transmittal, a list of principal officials and the Department's organization chart. The **Financial Section** includes the independent auditors' report, management's discussion and analysis, basic financial statements, notes to the financial statements, required supplementary information, as well as other supplementary information. The **Statistical Section** includes additional financial information and transportation data presented on a multi-year comparative basis.

Arizona Revised Statutes, §41-1279.03, requires the State Auditor General to "conduct or cause to be conducted at least biennial financial and compliance audits of financial transactions and accounts kept by or for all state agencies subject to the single audit act of 1984 (P.L. 98-502)." In fulfillment of this requirement, the Department prepared this CAFR, for the fiscal year ended June 30, 2005, and contracted with the independent public accounting firm of Deloitte & Touche LLP to audit the financial statements.

The objective of the independent audit is to provide a reasonable assurance that the financial statements are free from material misstatement. The independent audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statement presentation. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that the Department's financial statements for the fiscal year ended June 30, 2005, are fairly presented in conformity with accounting principles generally accepted in the United States of America (GAAP). The independent auditors' report is presented as the first component of the financial section of this report.

GAAP require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The Department's MD&A can be found immediately following the report of the independent auditors, beginning on page 3.

The CAFR includes all funds used to record the financial activity of the Department. Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the Department.

To provide a reasonable basis for making these representations, the Department has established a comprehensive internal control framework that is designed both to protect the Department's assets from loss, theft, or misuse and to compile sufficiently reliable information for the preparation of the financial statements in conformity with GAAP. The Department's internal control includes both automated controls, which are an integral component of the



2001 Award Recipient

financial accounting system, and comprehensive policies and procedures. In addition, the Department's Office of Audit and Analysis is an independent unit that reviews accounting controls and performs operational audits of the various divisions and units of the Department. Because the cost of internal controls should not outweigh their benefits, the Department's comprehensive framework of internal control has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatements.

To the best of our knowledge and belief, this financial report is complete and reliable in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of the various funds. All disclosures necessary to enable the reader to gain an understanding of the Department's financial activities have been included.

Profile of the Department

The Department was established by the State Legislature in July 1974 by combining the former Arizona Highway Department (originally established in 1927) and the State Department of Aeronautics (originally established in 1962). The Department is not legally separate from the State of Arizona's primary government. The Department's mission is to provide products and services for a safe, efficient, cost-effective transportation system that links Arizona to the global economy, promotes economic prosperity and demonstrates respect for Arizona's environment and quality of life. The Arizona Department of Transportation serves as the State's public agency to plan, develop, maintain and operate facilities for the efficient movement of people and goods by surface and air throughout the State. The Department has statutory responsibility for carrying out its programs under Arizona Revised Statutes, Titles 28, 35 and 41.

The Department receives guidance in capital planning and program development from a seven-member Transportation Board of the State of Arizona Department of Transportation (Transportation Board) appointed by the Governor. The Transportation Board is responsible for the annual update of the Five-Year Transportation Facilities Construction Program and awards contracts each month for highway projects. This program is a result of a transportation assessment to determine how best to safely and efficiently move goods, services and people throughout Arizona. The Transportation Board also has authority for the issuance of highway revenue and transportation excise tax bonds, grant anticipation notes, board funding obligations and approval of privatization agreements for toll facilities.

The Department is organized into four operating divisions supported by a Planning Division and a Transportation Services Group. The four operating divisions include: Intermodal Transportation Division, Motor Vehicle Division, Aeronautics Division and Public Transportation Division. The Intermodal Transportation Division is responsible for the management and maintenance of the existing State highway system and related facilities as well as the location, design and construction of new highways and facilities that are a part of the state highway system. The Motor Vehicle Division regulates motor vehicles in the State, processes motor vehicle registrations and drivers' license applications, issues certificates of title for motor vehicles and also operates 22 ports-of-entry. The Aeronautics Division coordinates general aviation in the State and is responsible for registering and licensing all general aviation aircraft, conducting the local airports grant program and representing the State at air service hearings. The Public Transportation Division is responsible for designing and managing certain rural transit programs to meet non-urbanized public, elderly and disabled transportation needs statewide. With the design and construction of the light rail program in Phoenix, the Public Transportation Division is also responsible for ensuring safety and security throughout the implementation and construction. The Transportation Planning Division is responsible for the planning of the statewide transportation system including highways and airports, and produces an annually updated Five-Year Transportation Facilities Construction Program for the Transportation Board, from which the Transportation Board establishes the priorities for highway and airport projects within the State. In addition, the Department has a Transportation Services Group that provides support to the Department's operating and other divisions. Overall, the Department employs approximately 4,500 persons.

Budgetary Controls Upon receipt of the operating budget appropriations bill, allocations are made to organizational levels within each division. The result is a detailed operating budget that guides the divisions and programs in their financial operation. State funding for the Five-Year Transportation Facilities Construction Program is included in the capital outlay appropriations bill, as a lump-sum budget without identifying individual projects. In the land, building and improvements portion of that bill, each separate building project is identified for control purposes. This bill also provides funding for building renewal purposes.

The budgets are prepared on a cash basis except that liabilities (encumbrances) incurred before the end of the fiscal year and paid within the next calendar month are charged against that prior fiscal year's budget. With a few exceptions, such as the capital budgets, highway maintenance and special line items, State appropriations typically lapse at the end of the fiscal year.

The Department relies on the Arizona Financial Information System (AFIS) to control total expenditures by appropriation. In addition, the Department utilizes several control features in its internal accounting system (ADVANTAGE™) to ensure budgetary compliance and management control. These features include: encumbrance and pre-encumbrance capabilities, appropriation allocation and control capabilities to the expense budget and organization unit level, and management control reports from the expense budget/organizational unit level, with summary reporting capabilities by program, division or appropriation.

Factors Affecting Financial Condition

Arizona Economy Fiscal year 2005 saw the Arizona economy strengthen to levels not seen since the late 1990's. Arizona saw significant growth in both employment and population. The state housing market mirrored much of the national housing market with strong home price appreciation. This appreciation led consumers to feel the "wealth effect" and resulted in higher levels of retail and construction spending. Low interest rates generated near record level new home sales and the hospitality industry saw tourism numbers return to near pre-September 11, 2001 levels. All of this strength in the Arizona economy overshadowed the record level fuel prices.

Two of the Department's three main funding sources, the Highway User Revenue Fund (HURF) and the Maricopa County Transportation Excise Tax, posted strong gains in fiscal year 2005. The HURF totaled \$1.25 billion, an increase of 5.4 percent over fiscal year 2004 and 1.4 percent above the forecast. Maricopa County Transportation Excise Tax collections totaled \$316.8 million, an increase of 9.8 percent over fiscal year 2004 and 3.2 percent above the forecast. The HURF revenue year-over-year growth was slightly below the fiscal year 2004 growth level while the Maricopa County Transportation Excise Tax collections posted the strongest year-over-year growth rate since fiscal year 1996.

The Arizona economy often lags the rest of the nation during recessionary periods but outperforms most of the nation during economic growth periods. Arizona's growth in employment and population was among the top five states during fiscal year 2005. Arizona saw significant job growth in the construction and business services sectors; however, it has yet to regain all the jobs lost in the manufacturing industry during the fiscal years 2000 and 2001 economic downturn.

The Department's fiscal year 2006 HURF estimate totals \$1.3 billion, an increase of 4.9 percent over fiscal year 2005. The HURF average compound growth rate for fiscal years 1996 through 2005 was 4.2 percent. The distribution of HURF revenues in fiscal year 2006 is estimated to be as follows: State Highway Fund \$626.1 million; Arizona cities and towns \$379.7 million; Arizona counties \$236.6 million; Department of Public Safety \$59.6 million; Economic Strength Project Fund \$1.0 million; and the Motor Vehicle Division for the registration compliance \$0.6 million. An additional \$2.7 million will be diverted from the General Fund's (State Highway Fund) share of HURF vehicle license tax revenues to the Department of Public Safety's Parity Compensation Fund.

Maricopa County Transportation Excise Tax revenues are projected to reach \$339.6 million in fiscal year 2006, a year-over-year increase of 7.2 percent. Fiscal year 2006 is projected to see somewhat slower growth compared to fiscal year 2005 due mainly to slower consumer spending brought on by higher interest rates and fuel prices. The Maricopa County Transportation Excise Tax average compound growth rate for fiscal years 1996 through 2005 was 6.9 percent.

The Department's third major funding source, federal funds, is also expected to see healthy increases in funding over the next several years. On August 10, 2005, President Bush signed the Safe, Accountable, Flexible, Efficient Transportation Equity Act: a Legacy for Users (SAFETEA-LU), a multi-year transportation funding bill. Under the bill, Arizona is expected to receive approximately 40% more in average apportionments for the period FY 2004 – 2009 than it received under the prior reauthorization bill (TEA-21) for the years 1998 – 2003. On an inflation-adjusted basis, this increase should result in a 17-20 percent higher funding level.

Planned Construction Activity In June 2005, the Transportation Board approved a \$5.1 billion highway construction program as part of the Five-Year Transportation Facilities Construction Program for fiscal years 2006 through 2010. This program provides funding for highway facilities on the National Highway System and the statewide system, as well as the new Maricopa County Regional Transportation Plan and the completion of the Maricopa Association of Governments (MAG) Life Cycle Program. The Five-Year Transportation Facilities Construction Program includes approximately: \$2.8 billion for freeway and expressway construction in Maricopa County (funded in large part from the Maricopa County Regional Area Road Fund) and \$2.3 billion for statewide projects. Programmatically, the Department expects to spend \$3.8 billion for system improvements, \$526 million for system management and \$837 million for system preservation.

The current Regional Freeway Program in Maricopa County will have opened 138 miles of new freeways by the end of fiscal year 2008. Currently, 114 miles have been opened to traffic since 1995, 16 more miles are under construction and 8 miles are planned.

On November 2, 2004, Maricopa County's voters approved Proposition 400 which extends the one-half cent sales tax for another 20 years through December 31, 2025. The sales tax extension will be used for construction of new freeways, widening of existing freeways and highways, improvements to the arterial street system, regional bus service and other special transportation services, and high capacity transit services such as light rail, bus rapid transit and express buses.

Since the end of the fiscal year, the Department has begun to see a disturbing trend in the cost of recently-bid construction projects. For a number of such projects, material and labor price increases, and in some cases shortages, have resulted in materially higher bid prices than those estimated by the Department. How long this trend will continue, and the potential impact this trend may have on the Board's Five-Year Transportation Facilities Construction Program, cannot yet be determined.

As part of the Five-Year Transportation Facilities Construction Program, the Transportation Board also adopted a \$665 million Five-Year Airport Development Program that includes 1,049 projects at general aviation and air carrier airports located throughout the State.

Other Information

Single Audit The Department is required to undergo an annual Single Audit in accordance with the provisions of the Single Audit Act Amendments of 1996 and the U.S. Office of Management and Budget Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations." The Department's Single Audit information is included in the Single Audit of the State of Arizona for the fiscal year ended June 30, 2005.

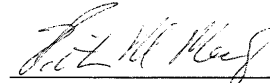
A requirement of the Single Audit is to ensure that adequate internal control is in place and that the Department is in compliance with applicable Federal laws and regulations. The United States Department of Transportation's (U.S. DOT) Inspector General has reviewed the internal controls on several occasions. The U.S. DOT auditors typically rely on the Department's internal audit staff in determining the scope of their review.

Awards The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Arizona Department of Transportation for its Comprehensive Annual Financial Report for the fiscal year ended June 30, 2004. This was the fifteenth consecutive year that the Department has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

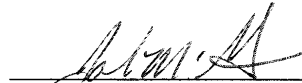
A Certificate of Achievement is valid for a period of one year only. We believe our current Comprehensive Annual Financial Report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

Acknowledgements We would like to express our sincere appreciation to the many individuals whose dedicated efforts have made this report possible. A special note of thanks is extended to the staff of Fiscal Operations whose commitment, professionalism, and dedicated efforts contributed to the timely preparation of the fiscal year 2005 Comprehensive Annual Financial Report.

Respectfully Submitted,



Victor M. Mendez, Director
Arizona Department of Transportation



John E. McGee, Chief Financial Officer
Arizona Department of Transportation

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Arizona
Department of Transportation

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2004

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

Arizona Department of Transportation List of Principal Officials

Victor M. Mendez

Director

David P. Jankofsky

Deputy Director

John A. Bogert

Chief of Staff

Sam M. Elters

State Engineer
Intermodal Transportation Division

Stacey K. Stanton

Assistant Director
Motor Vehicle Division

Dale J. Buskirk

Assistant Director
Transportation Planning Division

James D. Dickey

Assistant Director
Public Transportation Division

Barclay L. Dick

Assistant Director
Aeronautics Division

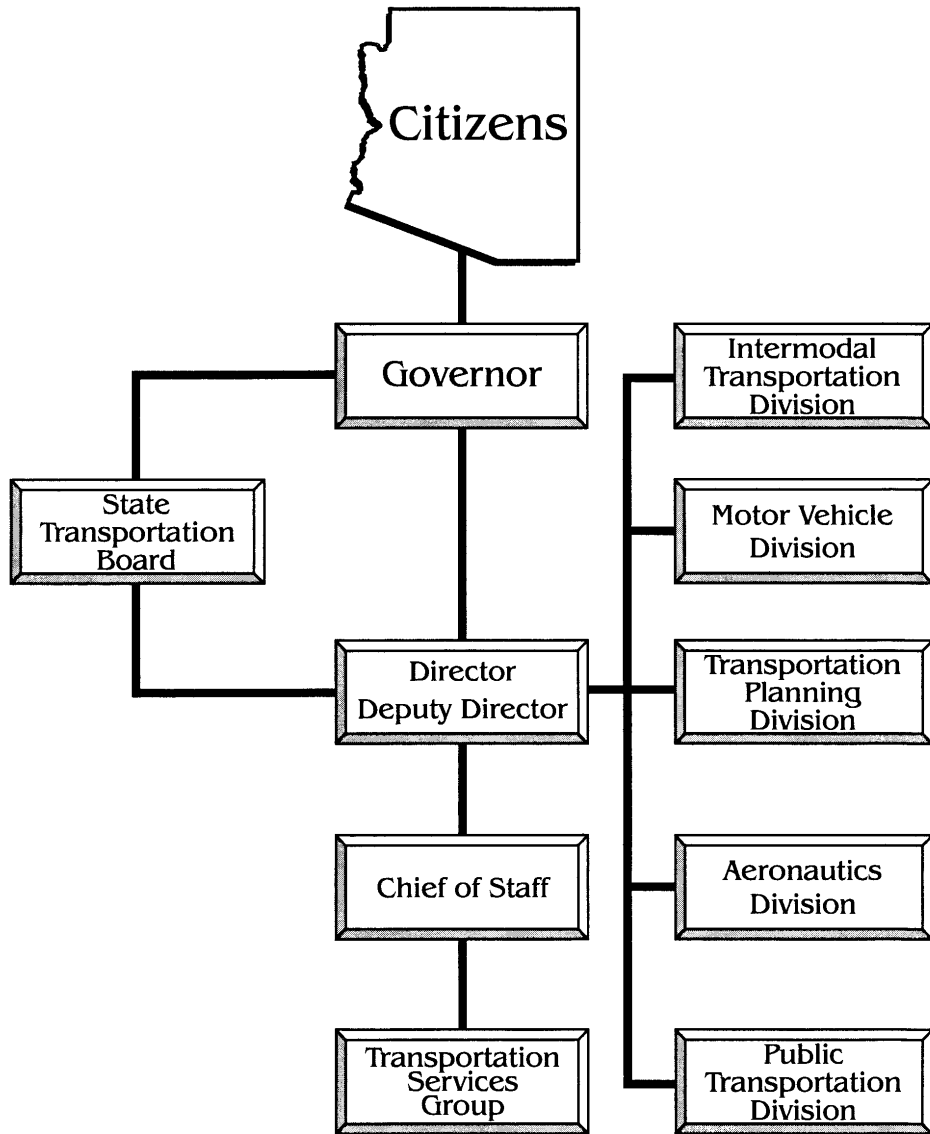
John E. McGee

Chief Financial Officer

Arizona State Transportation Board

Member	Counties	Term Expires
Dallas Gant, Chairman	District 1 (Maricopa County)	2006
Richard Hileman, Vice Chairman	District 6 (Yavapai, Yuma, Mohave, and LaPaz Counties)	2006
James W. Martin	District 3 (Cochise, Greenlee and Santa Cruz Counties)	2007
Joe Lane	District 1 (Maricopa County)	2008
S. L. Schorr	District 2 (Pima County)	2009
Delbert Householder	District 4 (Gila, Graham and Pinal Counties)	2010
Robert M. Montoya	District 5 (Navajo, Apache and Coconino Counties)	2011

State of Arizona Department of Transportation Organization Chart



FINANCIAL SECTION



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INDEPENDENT AUDITORS' REPORT

The Honorable Janet Napolitano
Governor of the State of Arizona, and
Members of the Legislature

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Arizona Department of Transportation (the "Department"), as of and for the year ended June 30, 2005, which collectively comprise the Department's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on the respective financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements of the Department of the State of Arizona (the "State"), are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only that portion of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State as of June 30, 2005, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the Department as of June 30, 2005, and the respective changes in financial position and respective cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Member of
Deloitte Touche Tohmatsu

The management's discussion and analysis, budgetary comparison information, and infrastructure assets reported using the modified approach as listed in the table of contents are not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of Department's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

Our audit was conducted for the purpose of forming an opinion on the Department's respective financial statements that collectively comprise the Department's basic financial statements. The introductory section, combining and individual nonmajor fund financial statements, and statistical tables are presented for purposes of additional analysis and are not a required part of the basic financial statements. This supplementary information is the responsibility of the Department's management. The combining and individual nonmajor fund financial statements have been subjected to the auditing procedures applied by us in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory section and statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

In accordance with Government Auditing Standards, we have also issued our report dated October 31, 2005, on our consideration of Department's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

DeBette & Touche LLP
October 31, 2005

Arizona Department of Transportation
Management's Discussion and Analysis
June 30, 2005

As management of the Arizona Department of Transportation (Department), we offer readers of the Department's financial statements this narrative overview and analysis of the financial activities of the Department for the fiscal year ended June 30, 2005. We encourage readers to consider the information presented here in conjunction with the letter of transmittal, which can be found on pages i-v, and the Department's basic financial statements, which begin on page 15 with the accompanying notes and Required Supplementary Information (RSI).

Financial Highlights

Government-wide:

- The net assets of the Department at the close of the fiscal year are \$11.6 billion, compared to \$10.9 billion for fiscal year 2004, an increase of 6.5 percent. Of this amount, \$234.3 million represents *unrestricted net assets* and may be used to meet the Department's ongoing obligations to citizens and creditors as compared to \$208.9 million in 2004.
- The Department's investment in capital assets, net of related debt, is \$10.8 billion, compared to \$10.2 billion for fiscal year 2004, an increase 5.9 percent. The Department's capital assets are \$12.7 billion, compared to \$12.0 billion for fiscal year 2004, an increase 5.1 percent. This increase is primarily attributable to the reduction of outstanding debt.
- The Department's non-current liabilities are \$2.0 billion, compared to \$2.0 billion in 2004. The Department retired \$9 million more in bonds than were issued. No new transportation excise tax revenue bonds were issued due to the scheduled expiration of the tax.

Fund Level:

- As of the close of the fiscal year, the governmental funds of the Department reported combined ending fund balances of \$537 million, as compared to \$434 million in 2004, a 23.7 percent increase over the prior fiscal year. The total reserved fund balance is \$447 million; of this, \$419 million (93.8 percent) is reserved for capital projects. Approximately \$90.5 million (16.8 percent) is available for spending at the government's discretion (unreserved fund balance) as compared to \$69 million (15.9 percent) in 2004. At the end of the fiscal year, the unreserved fund balance for the General Fund (State Highway Fund) was \$57 million.
- The proprietary funds reported net assets at year-end of \$65.6 million, as compared to \$65.6 million in 2004. There was a decrease of \$36 thousand due to a net loss in the Arizona Highways Magazine Fund caused by a decline in readership and several changes in cost recognition and reserve policies.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction of the Department's basic financial statements. The Department's basic financial statements consist of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other Required Supplementary Information in addition to the basic financial statements.

Government-wide Financial Statements (Reporting the Department as a Whole)

The government-wide financial statements are designed to present an overall picture of the financial position of the Department. These statements consist of the statement of net assets and the statement of activities and are prepared using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The statement of net assets combines and consolidates the Department's current financial resources with capital assets and long-term obligations. This statement includes all of the Department's non-fiduciary assets and liabilities. Net assets are the difference between the Department's assets and liabilities, and represent one measure of the Department's financial health.

Arizona Department of Transportation
Management's Discussion and Analysis
June 30, 2005

- An increase or decrease in the Department's net assets from one year to the next is an indicator of whether its financial health is improving or declining.
- Other indicators of the Department's financial health include the condition of its roads and bridges (infrastructure) and economic trends affecting the Department's future tax revenues.

The statement of activities focuses on both the gross and net cost of various activities (governmental and business-type); these costs are paid by the Department's general tax and other revenues. This statement summarizes the cost of providing specific Department services, and includes all current year revenues and expenses.

The statement of net assets and the statement of activities divide the Department's activities into two types:

Governmental Activities

The Department's basic services are reported here, including administration, aeronautics, highway, highway maintenance, motor vehicle division and other activities. Taxes, fees, and federal grants finance most of these activities.

Business-type Activities

Activities for which the Department charges a fee to customers to pay most or all of the costs of certain services it provides are reported as business-type activities. The Department's *Arizona Highways Magazine* and Highway Expansion and Extension Loan Program (HELP) are reported here.

The government-wide financial statements can be found on pages 15-16 of this report.

This report includes two schedules (Exhibit 3.1 and Exhibit 4.1) that reconcile the amounts reported on the governmental fund financial statements (prepared using the modified accrual basis of accounting and current financial resources measurement focus) with governmental activities (prepared using the accrual basis of accounting and economic resources measurement focus) on the appropriate government-wide statements. The following summarizes the impact of utilizing Governmental Accounting Standards Board Statement 34 (GASB 34) reporting:

- Capital assets used in governmental activities are not reported on governmental fund statements.
- Other long-term assets that are not available to pay for current period expenditures are not reported on governmental fund statements.
- Internal service fund activities are reported as governmental activities, but reported as proprietary funds in the fund financial statements.
- Bond issuance costs are capitalized and amortized to expense as governmental activities, but reported as expenditures in the governmental fund statements.
- Unless due and payable, long-term liabilities, such as capital lease obligations, compensated absences, notes payable and others, only appear as liabilities on the government-wide statements.
- Capital outlay spending results in capital assets on the government-wide statements, but is reported as expenditures on the governmental fund statements.
- Bond and note proceeds result in liabilities on the government-wide statements, but are recorded as other financing sources on the governmental fund statements.
- Certain other outflows represent either increases or decreases in liabilities on the government-wide statements, but are reported as expenditures on the governmental fund statements.

Fund Financial Statements (Reporting the Department's Major Funds)

The fund financial statements begin on page 17 and provide detailed information about the major individual funds. A fund is an accounting entity with a self-balancing set of accounts that the Department uses to keep track of specific sources of funding and spending for a particular purpose. The Department, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the Department can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental Funds. A majority of the Department's activities are reported in governmental funds. Reporting of these funds focuses on how financial resources flow in to and out of the funds, and amounts remaining at year-end for future spending. Governmental funds are accounted for using the modified accrual basis of accounting, which measures cash and other assets that can be readily converted to cash. The governmental fund statements provide a detailed short-term view of the Department's general governmental operations and the basic services it provides. This information should help determine whether there are more or less current financial resources available for the Department's programs. The reconciliation following the fund financial statements explains the differences between the government's activities, reported in the government-wide statement of activities, and the governmental funds.

The Department maintains fifteen individual governmental funds. Information is presented separately in the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances for the General Fund (State Highway Fund), Maricopa Regional Area Road Construction Fund, Motor Vehicle Division Clearing Fund, Highway User Revenue Fund, Debt Service Fund and Capital Projects Fund which are considered to be major funds. Data from the other nine governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds are provided in the form of combining statements elsewhere in this report.

The legislature appropriates an annual budget for the Department's General Fund (State Highway Fund). The Schedule of Revenues and Expenditures – Budget and Actual has been provided for the General Fund (State Highway Fund) to demonstrate compliance with this budget and is presented as Required Supplementary Information.

The governmental funds financial statements can be found on pages 17-24 of this report.

Proprietary Funds. When the Department charges customers for the services it provides, these services are generally reported in proprietary funds. Proprietary funds (enterprise and internal service) utilize full accrual accounting, the same method used by private sector businesses. Enterprise funds report activities that provide supplies and services to outside customers, other agencies or to other divisions of the Department. The Department's enterprise funds are the *Arizona Highways Magazine* Fund and Highway Expansion and Extension Loan Program Fund. The internal service fund reports activities that provide supplies and services for the Department's other programs and activities and other state agencies. The Equipment Fund is the Department's only internal service fund. Internal service fund activities are reported as governmental activities on the government-wide statements.

The proprietary funds financial statements can be found on pages 25-27 of this report.

Fiduciary Funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the Department's own programs.

The fiduciary fund financial statement can be found on page 28.

Notes to the Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 29-52 of this report.

Required Supplementary Information. In addition to the basic financial statements including accompanying notes, this section presents certain Required Supplementary Information concerning the Department's Schedule of Revenues and

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Expenditures – Budget and Actual for the General Fund (State Highway Fund) and the modified approach to reporting infrastructure assets. Required Supplementary Information can be found on pages 53-60 of this report.

Supplementary Information. Other Supplementary Information includes the combining statements for the non-major governmental funds, agency funds and capital assets and is presented immediately following the Required Supplementary Information on budget and infrastructure assets. Combining and individual fund statements and schedules can be found on pages 61-69 of this report.

Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of the Department's financial health. The following tables, graphs and analysis discuss the financial position and changes to financial position for the Department as a whole as of and for the fiscal years ended June 30, 2005 and 2004.

The Department's combined net assets increased by \$711 million over the course of this fiscal year's operations, an increase of 6.5 percent. The net assets of the governmental activities increased by \$711 million or 6.6 percent and business-type activities decreased by \$33 thousand or .1 percent.

The following table reflects the condensed Statement of Net Assets as of June 30:

	Governmental Activities		Business-type Activities		Total	
	2005	2004	2005	2004	2005	2004
Assets:						
Current and other assets	\$ 964,696,614	\$ 826,944,375	\$215,449,199	\$211,482,635	\$ 1,180,145,813	\$ 1,038,427,010
Capital assets	<u>12,650,004,961</u>	<u>12,032,459,953</u>	<u>499,474</u>	<u>810,011</u>	<u>12,650,504,435</u>	<u>12,033,269,964</u>
Total assets	<u>13,614,701,575</u>	<u>12,859,404,328</u>	<u>215,948,673</u>	<u>212,292,646</u>	<u>13,830,650,248</u>	<u>13,071,696,974</u>
Liabilities:						
Other liabilities	238,154,132	210,502,363	3,791,948	4,124,920	241,946,080	214,627,283
Non-current liabilities	1,869,530,670	1,852,874,536	146,587,988	142,565,681	2,016,118,658	1,995,440,217
Total liabilities	2,107,684,802	2,063,376,899	150,379,936	146,690,601	2,258,064,738	2,210,067,500
Net assets:						
Invested in capital assets, net of related debt	10,780,474,291	10,179,585,417	499,474	810,011	10,780,973,765	10,180,395,428
Restricted	491,994,682	408,410,333	65,273,296	63,899,875	557,267,978	472,310,208
Unrestricted	<u>234,547,800</u>	<u>208,031,679</u>	<u><204,033></u>	<u>892,159</u>	<u>234,343,767</u>	<u>208,923,838</u>
Total net assets	<u>\$11,507,016,773</u>	<u>\$10,796,027,429</u>	<u>\$ 65,568,737</u>	<u>\$ 65,602,045</u>	<u>\$11,572,585,510</u>	<u>\$10,861,629,474</u>

The total assets of the Department were \$13.8 billion, while total liabilities were \$2.2 billion, resulting in a net assets balance of \$11.6 billion. By far, the largest portion of the Department's net assets, \$10.8 billion (93.2 percent), was invested in capital assets (e.g., land, infrastructure, buildings, machinery and equipment), net of any related debt used to acquire those assets. The Department uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the Department's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other resources, since the capital assets themselves cannot be used to liquidate these liabilities.

As of June 30, 2005, the Department is able to report positive balances in all three categories of net assets for the governmental activities. The same situation held true for the prior fiscal year. The business-type activities reported a deficit in unrestricted net assets for the current year, although the balance was positive in the prior fiscal year.

There was a decrease of \$33 thousand in net assets for the Department's business-type activities. This decrease was due to a net loss in the Arizona Highways Magazine Fund combined with a gain in the Highway Expansion and Extension Loan Program fund.

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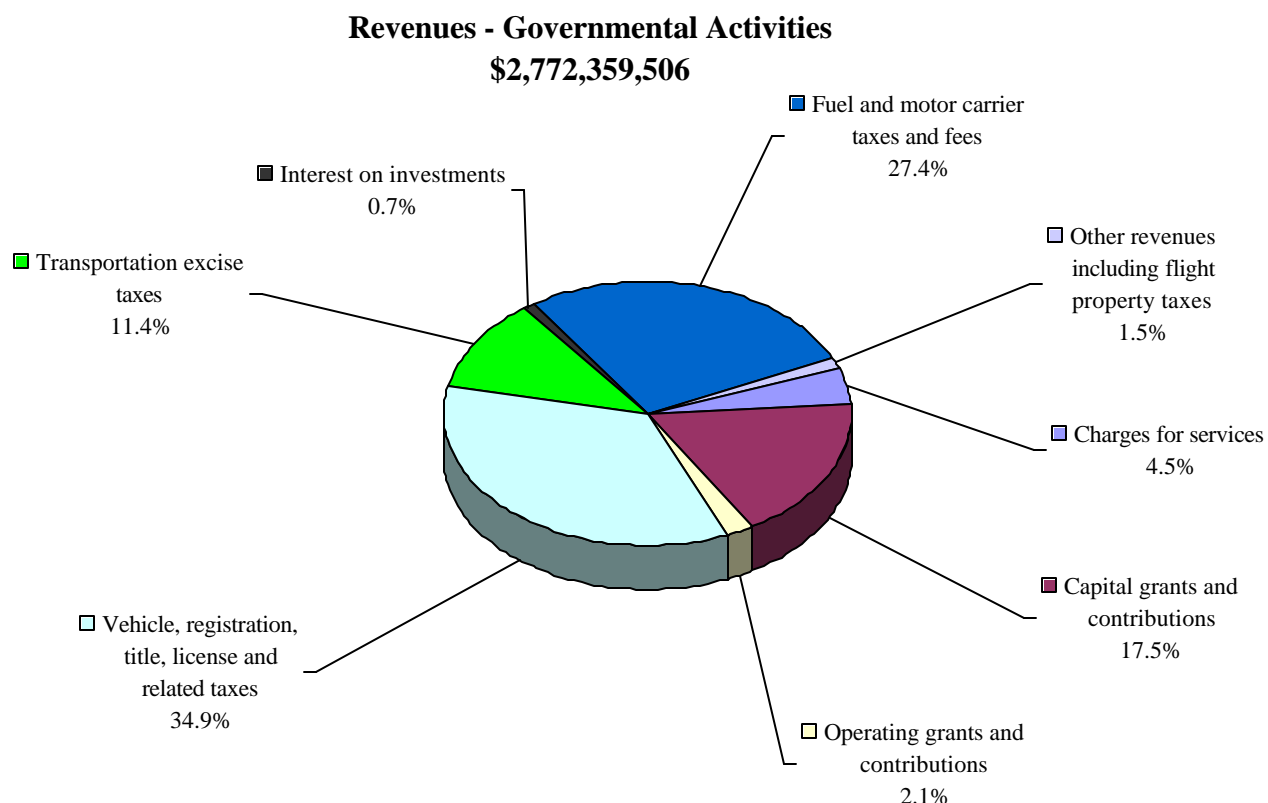
The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the Department's net assets changed during the year, compared to the prior year:

	Governmental Activities		Business-type Activities		Total	
	2005	2004	2005	2004	2005	2004
Revenues:						
Program revenues:						
Charges for services	\$ 126,267,181	\$ 118,225,054	\$ 11,452,006	\$ 12,799,883	\$ 137,719,187	\$ 131,024,937
Operating grants and contributions	58,947,746	44,007,905	-	-	58,947,746	44,007,905
Capital grants and contributions	484,275,728	418,174,005	-	-	484,275,728	418,174,005
General revenues:						
Transportation excise taxes	316,805,562	288,599,800	-	-	316,805,562	288,599,800
Vehicle, registration, title, license and related taxes	966,884,699	901,023,518	-	-	966,884,699	901,023,518
Fuel and motor carrier taxes and fees	759,632,832	712,039,873	-	-	759,632,832	712,039,873
Flight property taxes	13,180,039	6,320,722	-	-	13,180,039	6,320,722
Interest on investments	19,245,241	8,352,046	2,764,337	1,587,588	22,009,578	9,939,634
Other	27,120,478	24,774,776	380,488	504,612	27,500,966	25,279,388
Total revenues	<u>2,772,359,506</u>	<u>2,521,517,699</u>	<u>14,596,831</u>	<u>14,892,083</u>	<u>2,786,956,337</u>	<u>2,536,409,782</u>
Expenses:						
Administration	42,297,877	57,702,625	-	-	42,297,877	57,702,625
Aeronautics	9,803,605	7,512,258	-	-	9,803,605	7,512,258
Highway	72,665,070	48,797,165	-	-	72,665,070	48,797,165
Highway Maintenance	105,036,826	95,641,623	-	-	105,036,826	95,641,623
Motor Vehicle	91,676,147	86,845,369	-	-	91,676,147	86,845,369
Other	6,871,015	9,814,863	-	-	6,871,015	9,814,863
Non-capital, including asset preservation	209,901,662	378,788,704	-	-	209,901,662	378,788,704
Distributions to Arizona counties and cities	1,086,955,131	1,022,767,761	-	-	1,086,955,131	1,022,767,761
Distributions to other state agencies	306,852,517	161,029,210	-	-	306,852,517	161,029,210
Intergovernmental	42,440,134	39,205,377	-	-	42,440,134	39,205,377
Interest on long-term debt	86,870,178	89,430,886	-	-	86,870,178	89,430,886
Arizona Highways Magazine	-	-	10,270,407	10,006,670	10,270,407	10,006,670
Highway Expansion and Extension Loan Program	-	-	4,359,732	4,413,701	4,359,732	4,413,701
Total expenses	<u>2,061,370,162</u>	<u>1,997,535,841</u>	<u>14,630,139</u>	<u>14,420,371</u>	<u>2,076,000,301</u>	<u>2,011,956,212</u>
Change in net assets	710,989,344	523,981,858	<33,308>	471,712	710,956,036	524,453,570
Net assets - July 1	<u>10,796,027,429</u>	<u>10,272,045,571</u>	<u>65,602,045</u>	<u>65,130,333</u>	<u>10,861,629,474</u>	<u>10,337,175,904</u>
Net assets - June 30	<u>\$ 11,507,016,773</u>	<u>\$ 10,796,027,429</u>	<u>\$ 65,568,737</u>	<u>\$ 65,602,045</u>	<u>\$ 11,572,585,510</u>	<u>\$ 10,861,629,474</u>

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Governmental Activities:

The following chart depicts revenues of the governmental activities for the fiscal year ended June 30, 2005:



\$2.5 billion (or 91.2 percent) of the Department's revenues are from the following four revenue sources:

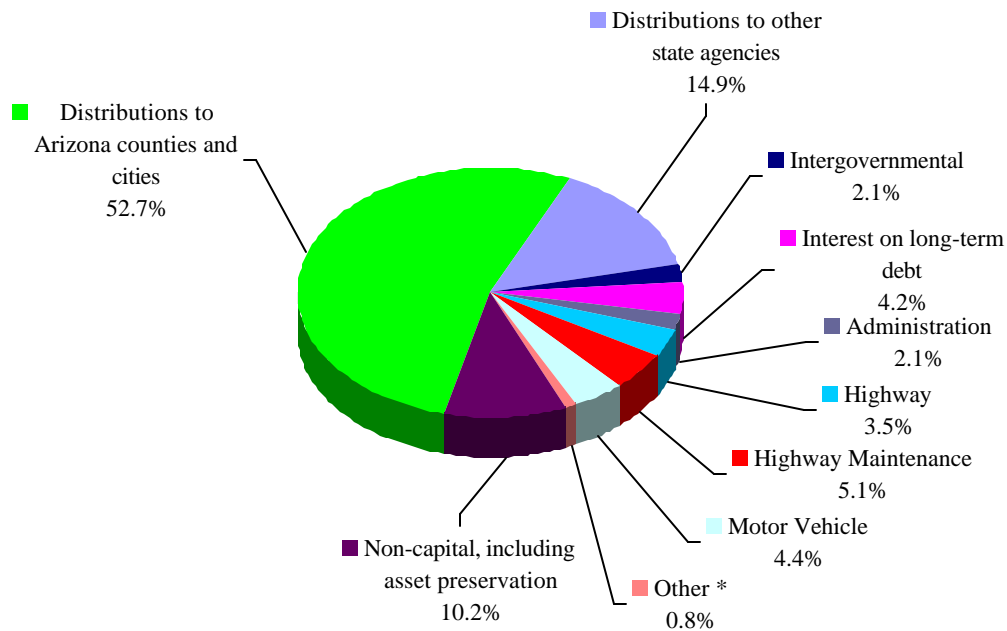
- Vehicle, registration, title, license and related taxes comprise the Department's largest revenue source of \$966.9 million (34.9 percent).
- Fuel and motor carrier taxes and fees represent the Department's second largest revenue source of \$759.6 million (27.4 percent).
- Capital grants and contributions total \$484.3 million (17.5 percent).
- Transportation excise taxes are the Department's fourth largest revenue source of \$316.8 million (11.4 percent).

The Highway User Revenue Fund (HURF) and the Maricopa County Transportation Excise Tax both posted strong gains in fiscal year 2005. The HURF revenue year-over-year growth was slightly below the fiscal year 2004 growth level while the Maricopa County Transportation Excise Tax collections posted the strongest year-over-year growth rate since fiscal year 1996. The growth in collections was broad based, posting gains over fiscal year 2004 for vehicle registration, gas tax, use fuel tax and motor carrier taxes because of the increase in the population, which tends to follow job growth.

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The following chart depicts expenses of the governmental activities for the fiscal year ended June 30, 2005:

Expenses - Governmental Activities
\$2,061,370,162



*Other includes expenses for Aeronautics and Other

\$1.6 billion (or 77.8 percent) of the Department's expenses were for the following:

- Distributions to Arizona counties and cities \$1,087.0 million (52.7 percent).
- Distributions to other state agencies \$307.0 million (14.9 percent).
- Non-capital, including asset preservation \$209.9 million (10.2 percent)

The increase in distributions to other state agencies was due to 2004 Senate Bill 1314 which required an additional \$118.0 million be transferred from fuel tax revenues to the State of Arizona General Fund. There was also a 6.3 percent increase in the distributions to Arizona counties and cities due to an increase in motor fuel tax and vehicle license tax collections.

Business-type Activities:

Net assets for business-type activities decreased by \$33 thousand in fiscal year 2005. Total revenues were \$14.6 million, with charges for services representing 78.5 percent and interest on investments 18.9 percent. The total expenses for business-type activities were \$14.6 million. Factors contributing to these results included:

- The Arizona Highways Magazine (AHM) had an operating deficit of \$1.4 million in fiscal year 2005. Two key factors contributed to this result. First, normal operations as reported utilizing the magazine's historical accounting practices resulted in a deficit of about \$550 thousand. The publishing industry continues an overall decline and the Magazine experienced a readership decline that approximated industry wide trends. Secondly, AHM introduced several new accounting policies, which lead to recognizing an additional \$850 thousand in expenses in 2005 that were incurred and deferred in fiscal year 2004 and prior years. AHM incurs project expenditures in advance of sales revenue for the associated project. Typical project costs include prepaid book royalties to authors, payments for writing and photography works from freelance contributors and payment for production costs for related product sales such as calendars, holiday cards and catalog items. These project costs are generally deferred until the future period in which the sales revenue is earned and recognized. The enterprise established new cost recognition and reserve policies to recognize in the current period deferred project expenditures when the likelihood of associated future revenues has been substantially delayed or impaired. For fiscal year 2005, the enterprise was able to achieve positive cash flow for the third time in eleven years and, despite the highly competitive business environment, expects positive cash flow again in fiscal year 2006.
- The Highway Expansion and Extension Loan Program had an increase in revenues of \$644 thousand. The interest on loans receivables decreased by 15 percent in fiscal year 2005 compared to a decrease of 9 percent in fiscal year 2004. Higher average interest rates on invested cash due to prevailing market conditions during fiscal year 2005 resulted in increased interest on investments of \$1.2 million for fiscal year 2005.

Financial Analysis of the Department's Funds

As previously mentioned, the Department uses fund accounting to ensure and demonstrate compliance with budgetary and legal requirements. The following is a brief discussion of financial highlights from the fund financial statements.

Governmental Funds. The focus of the Department's governmental funds financial statements (pages 17-24) is to provide information on near-term inflows, outflows, and balances of spendable resources. All major governmental funds are discretely presented on these financial statements, while the non-major governmental funds are combined into a single column. Combining statements for the non-major governmental funds may be found on pages 61-64.

As of the end of the fiscal year, the fund balances of the governmental funds totaled \$537.0 million, an increase of \$103.1 million over the previous fiscal year. Of this balance, \$90.0 million or 16.8 percent constitutes the unreserved fund balance, which was available for spending for the general purposes of the Department. The remaining fund balance of \$447.0 million, or 83.2 percent, was reserved for the following: 1) \$5.2 million for inventories, 2) \$20.0 million to liquidate an advance to the HELP Fund, 3) \$2.3 million to pay debt service, and 4) \$419 million to pay for capital projects.

The General Fund (State Highway Fund) is the primary operating fund of the Department. At the end of the current fiscal year, the unreserved fund balance of the General Fund (State Highway Fund) was \$57.1 million and the reserved fund balance was \$166.4 million. As a measure of the General Fund's (State Highway Fund) liquidity, it may be useful to compare both the unreserved fund balance and the total fund balance to the total fund expenditures. Unreserved fund balance represents 7.0 percent of total General Fund (State Highway Fund) expenditures, while total fund balance represents 27.5 percent of the same amount.

The Maricopa Regional Area Road Construction Fund (MRF) is a major special revenue fund that receives Maricopa County Transportation Excise Tax monies that are used for construction of certain state highways within Maricopa County. Total revenues collected in fiscal year 2005 were \$346.3 million; transportation excise revenue of \$316.8 million (or 91.5

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percent) was the bulk of the revenue. Of this revenue, \$204.9 million (or 64.7 percent) was used to pay the debt service for the Transportation Excise Tax Revenue Bonds.

The Debt Service Fund is used for the accumulation of resources for, and the payment of, general long-term debt principal and interest of the governmental funds. The other financing sources of \$374.2 million were transferred in from the General Fund (State Highway Fund) (\$104.5 million), the Capital Projects Fund (1.0), the MRF fund (\$204.9 million) and Grant Anticipation Notes Fund (\$63.8 million), and were used to pay the debt service payment of \$393.8 (principal \$301.9 million, and interest \$91.8 million) during the fiscal year. The remaining fund balance of \$2.2 million is restricted for future debt service payments.

The Capital Projects Fund is used to account for financial resources used for the acquisition or construction of major capital facilities of the governmental funds. During the fiscal year, the Department's expenditures were \$268.9 million. Capital outlay expenditure of \$236.4 million (87.9 percent) accounted for the majority of the expenditures. This expenditure for the acquisition and construction of new highways was converted to capital assets on the government wide statements. The fund balance increased by \$44.9 million (51.1) during this fiscal year.

Budget Variances

There were no significant differences between the Department's budgeted amounts and the actual expenditures for fiscal year 2005.

Capital Assets and Debt Administration

Capital Assets (See Note 5A to the financial statements for additional information):

The Department's investment in capital assets for its governmental and business-type activities as of June 30, 2005, amounts to \$12.7 billion (net of accumulated depreciation), a \$.6 billion increase over the previous fiscal year.

	Governmental Activities		Business-type Activities		Total	
	2005	2004	2005	2004	2005	2004
Land	\$ 1,875,770,486	\$ 1,858,113,828	\$ 7,900	\$ 7,900	\$ 1,875,778,386	\$ 1,858,121,728
Buildings and improvements	91,904,625	93,975,769	244,151	277,968	92,148,776	94,253,737
Improvements other than buildings	32,529,900	32,151,069	-	-	32,529,900	32,151,069
Mobile fleet and aircraft	45,923,112	38,477,108	-	-	45,923,112	38,477,108
Machinery and equipment	16,624,936	16,437,987	247,423	524,143	16,872,359	16,962,130
Infrastructure	8,863,627,692	8,591,370,633	-	-	8,863,627,692	8,591,370,633
Construction in progress	1,723,624,210	1,401,933,559	-	-	1,723,624,210	1,401,933,559
Total	<u>\$ 12,650,004,961</u>	<u>\$ 12,032,459,953</u>	<u>\$ 499,474</u>	<u>\$ 810,011</u>	<u>\$12,650,504,435</u>	<u>\$12,033,269,964</u>

As provided by accounting principles generally accepted in the United States (GAAP), the Department has elected to record its infrastructure assets using the modified approach, as defined in GASB Statement 34. Assets accounted for under the modified approach include 6,816 center lane miles (18,424 travel lane miles) and 4,608 bridges that the Department is responsible for maintaining.

The Five-Year Transportation Facilities Construction Program (Program) is a dynamic instrument and adjustments are made to the annual plans based on the needs of the Department to maintain the condition level of the roads and bridges at a level equal to, or greater than, the goals established by the Department. In addition, not only are adjustments made during the life of the Program, circumstances may require that refinements to the individual components of the Program be made during the fiscal year.

In comparing Estimated to Actual Expenditures, significant variances can occur. These variances are primarily due to the methodology used in the preparation of the Program. In this Program, the Estimated Expenditures for the current year are based on "programmed" projects, which may or may not be spent in the current year of the Program. "Programmed"

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expenditures consist of those items that are planned for the future and contracts have not yet been awarded. Furthermore, the Actual Expenditures will include projects that were "programmed" for a prior year's Estimated Expenditures but which did not occur, or were not completed, in the prior year.

The Department manages its roads using the Present Serviceability Rating (PSR), which measures the condition of the pavement and its ability to serve the traveling public. The PSR uses a five-point scale (5 excellent, 0 impassable) to characterize the condition of the roadway. The Department's serviceability rating goal is 3.23 for the overall system. The most recent assessment from the Transportation Material Technicians indicated that an overall rating of 3.8 was achieved for fiscal year 2005.

The Department manages its bridges using the Arizona Bridge Information and Storage System (ABISS). The Department determines the condition rating based on standards developed by the Federal Highway Administration and additional internal criteria. It is the policy of the Department to maintain a Condition Rating Index (CRI) of 92.5 percent or better. In fiscal year 2005, a CRI of 93.9 percent was obtained.

In addition to many smaller projects, each of the following major highway construction projects in excess of \$20 million were started during fiscal year 2005:

<u>Description</u>	<u>Contract Start Date</u>	<u>Contract Amount</u>	<u>Total Contract Expenditures</u>
Construction of State Route Loop 202 from Frye Road to Power Road in Maricopa County.	09/20/2004	\$58,869,154	\$ 21,746,738
Construction of State Route Loop 202 from Gilbert Road to Frye Road in Maricopa County.	11/10/2004	50,458,080	17,460,627
Construction on Interstate 60 at 59th Avenue and Glendale Avenue in Maricopa County.	11/22/2004	25,995,948	5,004,665
Construction at the interchange of State Route Loop 202 and Interstate 60 in Maricopa County.	04/18/2005	\$71,374,832	\$ 3,847,537

In addition to many smaller projects, the following major highway construction projects had expenditures in excess of \$15 million in fiscal year 2005. These expenditures include payments made to construction contractors as well as utility, design, right-of-way and landscaping costs.

<u>Description</u>	<u>Project Expenditures</u>
Construction of State Route Loop 202 from Power road to Elliot Road in Maricopa County.	\$ 34,236,011
Construction on State Route Loop 202 from Arizona Avenue to Gilbert Road in Maricopa County.	32,570,797
Construction of State Route Loop 202 from Frye Road to Power Road in Maricopa County.	28,601,165
Construction on State Route Loop 202 from Elliot Road to Baseline Road in Maricopa County.	24,317,032
Construction of State Route Loop 202 from Gilbert Road to Frye Road in Maricopa County.	23,689,258
Construction on State Route 85 to add a parallel road between Gila Bend and Interstate 10 to improve capacity and safety in Maricopa County.	23,319,197
Construction on State Route Loop 202 from Dobson Road to Arizona Avenue in Maricopa County.	20,601,415
Construction on State Route Loop 202 west of Higley Road to Power Road in Maricopa County.	19,689,959
Construction at the interchange of State Route Loop 202 and Interstate 60 in Maricopa County.	17,817,728
Construction on the Burro Creek Section of US 93 in Mohave County.	16,897,744
Construction on State Route 51 from Interstate 10 to Shea Boulevard in Maricopa County.	\$ 15,452,590

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Non-Current Liabilities (See Note 5G to the financial statements for additional information):

The Department's non-current liabilities for its governmental and business-type activities as of June 30, 2005, amounts to \$2.0 billion, an increase of \$20.7 million over the previous fiscal year.

Governmental Activities	2005	2004
Highway revenue bonds	\$ 1,161,355,000	\$ 1,017,360,000
Transportation excise tax revenue bonds	80,375,000	289,000,000
Grant anticipation notes	363,970,000	308,585,000
Premium on bonds	76,721,480	60,480,591
Compensated absences	11,726,637	11,023,013
Capital leases	5,909,829	1,120,965
Notes payable	169,472,724	165,304,967
Total Governmental Activities	<u>1,869,530,670</u>	<u>1,852,874,536</u>
Business-type Activities		
Compensated absences	133,522	151,215
Notes payable	146,454,466	142,414,466
Total Business-type Activities	<u>146,587,988</u>	<u>142,565,681</u>
Total Non-Current Liabilities	<u>\$2,016,118,658</u>	<u>\$ 1,995,440,217</u>

The revenue bonds have been sold in 36 separate issues between 1980 and 2005. All bonds outstanding as of June 30, 2005, are scheduled to mature on various dates, but not later than July 1, 2024. The bonds are obligations of the State Transportation Board and are not obligations of the State of Arizona.

Of the \$5.4 billion total in bonds issued between 1980 and 2005, \$1.3 billion, or approximately 24 percent, have been refunding issues to lower debt service costs. These efforts have resulted in cumulative debt service savings of \$74.6 million in current dollars and \$54.7 million on a present value basis.

The senior lien Highway User Revenue Fund (HURF) bonds have been rated AAA/Aa1 by Standard & Poor's Ratings Services and Moody's Investors Service, respectively. The Department's subordinate lien HURF bonds are rated AA/Aa2. The senior lien Regional Area Road Fund (RARF) bonds are rated AA/Aa2, while the subordinate lien RARF bonds are rated A/Aa3. The Grant Anticipation Notes are rated AA-/Aa3/AA with the additional rating provided by Fitch Ratings.

Arizona Revised Statutes, ARS 28-7678, authorized the Transportation Board to issue non-negotiable Board Funding Obligations (BFOs) for purchase by the Arizona State Treasurer. Laws 2005, Chapter 150 (HB 2123), authorized the Transportation Board to issue BFOs in the principal amount of \$200 million in any fiscal year from fiscal years 2006 through 2020 and that mature no later than four calendar years after the date of issuance. The distribution of this authority is \$60 million to the General Fund (State Highway Fund) and \$140 million to the Highway Expansion and Extension Loan Program (HELP) Fund. The BFOs are used to capitalize Arizona's State Infrastructure Bank, which allows the Department and political subdivisions to apply for loans from the HELP Fund established by this legislation.

In fiscal year 2005, the Department issued Highway Revenue Bonds totaling \$188,260,000 to (i) finance portions of the Transportation Board's Five-Year Transportation Facilities Construction Program, (ii) pay costs of issuing the bonds, and (iii) pay interest on any bonds issued for highway purposes. The Department also issued Grant Anticipation Notes totaling \$104,385,000 to (i) pay costs of the projects (as specified) and (ii) pay the costs of issuing the notes.

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Requests for Information

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with an overview of the Department's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Controller, Arizona Department of Transportation, 206 S. 17th Avenue, Phoenix, Arizona, 85007 or by visiting our website at [http://www.azdot.gov/Inside ADOT/fms](http://www.azdot.gov/Inside_ADOT/fms).

BASIC FINANCIAL STATEMENTS

Government-wide Financial Statements – include the Statement of Net Assets and Statement of Activities and uses the accrual basis of accounting for financial reporting.

Governmental Fund Financial Statements – include the Balance Sheet and Statement of Revenues, Expenditures and Changes in Fund Balances for the major governmental funds and uses the modified accrual basis of accounting for financial reporting. Also includes the reconciliations to the government-wide financial statements.

Proprietary Fund Financial Statements – include the Statement of Net Assets, Statement of Revenues, Expenses and Changes in Fund Net Assets and Statement of Cash Flows for the business-type activities and uses the accrual basis of accounting for financial reporting.

Statement of Fiduciary Net Assets – includes the Statement of Net Assets for assets being held for parties outside of the Department.

Notes to the Financial Statements

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Statement of Net Assets
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	Governmental Activities	Business-type Activities	Total
ASSETS			
Unrestricted cash on deposit with the State Treasurer	\$ 197,125,509	\$ 1,774,165	\$ 198,899,674
Receivables:			
Notes and loans	5,586,168	131,430,313	137,016,481
Subscriptions, net of allowance for doubtful accounts	-	396,137	396,137
Accrued interest	1,704,420	277,628	1,982,048
Taxes and fees	60,057,262	-	60,057,262
Other, net of allowance for doubtful accounts	14,118,717	59,907	14,178,624
Due from U.S. Government for reimbursable construction costs	40,074,217	-	40,074,217
Due from other state agencies	40,552	203,158	243,710
Internal balances	15,425,291	<15,425,291>	-
Inventories	8,028,257	1,137,120	9,165,377
Prepaid items	-	290,978	290,978
Deferred charges	14,510,632	-	14,510,632
Restricted cash on deposit with the State Treasurer	608,025,589	95,305,084	703,330,673
Capital assets not subject to depreciation (Note 5A)	12,463,022,388	7,900	12,463,030,288
Capital assets subject to depreciation, net of accumulated depreciation (Note 5A)	186,982,573	491,574	187,474,147
Total assets	<u>13,614,701,575</u>	<u>215,948,673</u>	<u>13,830,650,248</u>
LIABILITIES			
Accounts payable and other current liabilities	7,952,520	112,644	8,065,164
Accrued payroll and other accrued expenses	7,634,589	110,825	7,745,414
Contracts and retainage payable	86,860,821	-	86,860,821
Due to Arizona counties and cities	127,738,437	-	127,738,437
Due to other state agencies	7,967,765	-	7,967,765
Deferred revenues (Note 5C)	-	3,568,479	3,568,479
Non-current liabilities (Note 5G):			
Due within one year	198,145,790	133,522	198,279,312
Due in more than one year	1,671,384,880	146,454,466	1,817,839,346
Total liabilities	<u>2,107,684,802</u>	<u>150,379,936</u>	<u>2,258,064,738</u>
NET ASSETS			
Invested in capital assets, net of related debt	10,780,474,291	499,474	10,780,973,765
Restricted:			
Loans and other financial assistance	-	65,273,296	65,273,296
Debt service	3,051,797	-	3,051,797
Capital projects	488,942,885	-	488,942,885
Unrestricted	234,547,800	<204,033>	234,343,767
Total Net Assets	<u>\$ 11,507,016,773</u>	<u>\$ 65,568,737</u>	<u>\$ 11,572,585,510</u>

The notes to the financial statements are an integral part of this statement.

Arizona Department of Transportation
Statement of Activities
For the fiscal year ended June 30, 2005

Functions/Programs	Expenses	Program Revenues			Net <Expenses> Revenues
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental Activities:					
Administration	\$ 42,297,877	\$ -	\$ -	\$ -	\$ <42,297,877>
Aeronautics	9,803,605	919,327	4,203,044	-	<4,681,234>
Highway	72,665,070	-	12,421,228	484,275,728	424,031,886
Highway Maintenance	105,036,826	1,518,029	-	-	<103,518,797>
Motor Vehicle	91,676,147	113,506,009	-	-	21,829,862
Other	6,871,015	5,563,506	-	-	<1,307,509>
Non-capital, including asset preservation	209,901,662	-	-	-	<209,901,662>
Distributions to Arizona counties and cities	1,086,955,131	-	-	-	<1,086,955,131>
Distributions to other state agencies	306,852,517	-	-	-	<306,852,517>
Intergovernmental	42,440,134	4,760,310	42,323,474	-	4,643,650
Interest on long-term debt	86,870,178	-	-	-	<86,870,178>
Total governmental activities	<u>2,061,370,162</u>	<u>126,267,181</u>	<u>58,947,746</u>	<u>484,275,728</u>	<u><1,391,879,507></u>
Business-type Activities:					
Arizona Highways Magazine	10,270,407	8,443,339	-	-	<1,827,068>
Highway Expansion and Extension Loan Program	<u>4,359,732</u>	<u>3,008,667</u>	<u>-</u>	<u>-</u>	<u><1,351,065></u>
Total business-type activities	<u>14,630,139</u>	<u>11,452,006</u>	<u>-</u>	<u>-</u>	<u><3,178,133></u>
Total	<u>\$ 2,076,000,301</u>	<u>\$ 137,719,187</u>	<u>\$ 58,947,746</u>	<u>\$ 484,275,728</u>	<u>\$ <1,395,057,640></u>
			Governmental Activities	Business-type Activities	Total
Net <expenses>			\$ <1,391,879,507>	\$ <3,178,133>	\$ <1,395,057,640>
General revenues:					
Transportation excise taxes			316,805,562	-	316,805,562
Vehicle, registration, title, license and related taxes			966,884,699	-	966,884,699
Fuel and motor carrier taxes			759,632,832	-	759,632,832
Flight property taxes			13,180,039	-	13,180,039
Interest on investments			19,245,241	2,764,337	22,009,578
Sale of capital assets			18,391,623	-	18,391,623
Other			8,728,855	380,488	9,109,343
Total general revenues			<u>2,102,868,851</u>	<u>3,144,825</u>	<u>2,106,013,676</u>
Change in net assets			710,989,344	<33,308>	710,956,036
Net assets - July 1			<u>10,796,027,429</u>	<u>65,602,045</u>	<u>10,861,629,474</u>
Net assets - June 30			\$ 11,507,016,773	\$ 65,568,737	\$ 11,572,585,510

The notes to the financial statements are an integral part of this statement.

GOVERNMENTAL FUNDS

FINANCIAL STATEMENTS

MAJOR FUNDS

General Fund (State Highway Fund)

This fund is used to account for all financial transactions applicable to the general operations of the Department. The fund receives money from the Highway User Revenue Fund for vehicle registration, title, license and related fees and fuel and motor carrier taxes. Reimbursements for certain construction expenditures are received from the federal government, Arizona cities and counties, and other state agencies. The fund also receives interest and other revenues. The fund disburses money primarily for the engineering, construction, improvement and maintenance of state highways, parts of highways forming state routes and highways under cooperative agreements with the United States.

Maricopa Regional Area Road Construction Fund

This fund receives Maricopa County transportation excise tax monies collected by the Department of Revenue. These monies are used for the construction of certain state highways within Maricopa County.

Motor Vehicle Division Clearing Fund

This fund accounts for the collection and disbursement of Motor Vehicle Division revenues.

Highway User Revenue Fund

This fund collects motor vehicle and liquid use fuel taxes and receives certain Motor Vehicle Division revenues from the Motor Vehicle Division Clearing Fund. These monies are distributed to the State Highway Fund, the Department of Public Safety, the Arizona State Parks, the Economic Strength Project Fund, and incorporated cities and counties.

Debt Service Fund

This fund is used to administer all payments of principal and interest on bonds and notes issued by the Arizona Department of Transportation Board for Highway Revenue Bonds, Arizona Transportation Excise Tax Revenue Bonds, and Grant Anticipation Notes.

Capital Projects Fund

This fund is used to administer bond proceeds for Arizona Transportation Board Highway Revenue Bonds, Arizona Transportation Excise Tax Revenue Bonds, Grant Anticipation Notes and Board Funding Obligations. These monies are expended for the construction of federal, state and local highways within the state.

NON-MAJOR FUNDS

Other Governmental Funds are the non-major funds and are all special revenue funds. These funds can be found on Exhibit 9 and Exhibit 10.

Arizona Department of Transportation
Balance Sheet
Governmental Funds
June 30, 2005

		Special Revenue Funds			
		Maricopa	Motor		
		Regional	Vehicle		
	General	Area Road	Division		Highway
	Fund	Construction	Clearing		User
	(State Highway Fund)	Fund	Fund		Revenue
					Fund
ASSETS					
Unrestricted cash on deposit with the					
State Treasurer	\$ 161,158,006	\$ -	\$ -	\$ -	
Receivables:					
Accrued interest	792,688	70,913	-		129,640
Interfund (Note 5E)	97,335,975	20,430	742,860		18,219,355
Taxes and fees	-	-	6,838,718		53,218,544
Notes and loans	317,372	1,298,810	-		-
Other	5,493,250	6,833,171	-		-
Amounts due from:					
U.S. Government	32,227,677	1,991	-		-
Arizona counties and cities	-	-	-		-
Inventories	5,231,165	-	-		-
Advance to other funds	20,000,000	-	-		-
Deferred charges	-	-	8,134,859		-
Restricted cash on deposit with the State Treasurer	141,188,341	153,184,337	41,544,284		120,954,057
Total assets	<u>\$ 463,744,474</u>	<u>\$ 161,409,652</u>	<u>\$ 57,260,721</u>	<u>\$ 192,521,596</u>	
LIABILITIES AND FUND BALANCES					
Liabilities:					
Accounts payable	\$ 958,405	\$ 26,555	\$ 5,774,510	\$ 1,063	
Accrued payroll and other accrued					
expenditures	9,279,654	4,965	-		683
Contracts and retainage payable	53,584,625	26,178,929	-		-
Interfund payables (Note 5E)	5,500,624	85,000	21,354,518		97,222,524
Amounts due to:					
Arizona counties and cities	-	-	28,416,589		95,297,326
Other state agencies	373,636	-	1,387,752		-
Surety and rental deposits	715,303	-	327,352		-
Deferred revenue	317,372	1,298,810	-		-
Notes payable	169,472,724	-	-		-
Total liabilities	<u>240,202,343</u>	<u>27,594,259</u>	<u>57,260,721</u>	<u>192,521,596</u>	
Fund balances:					
Reserved for:					
Inventories	5,231,165	-	-		-
Advance to other funds	20,000,000	-	-		-
Debt service	-	-	-		-
Capital projects	141,188,341	133,815,393	-		-
Unreserved reported in:					
General fund	57,122,625	-	-		-
Non-major special revenue funds	-	-	-		-
Total fund balances	<u>223,542,131</u>	<u>133,815,393</u>	<u>-</u>	<u>-</u>	
Total liabilities and fund balances	<u>\$ 463,744,474</u>	<u>\$ 161,409,652</u>	<u>\$ 57,260,721</u>	<u>\$ 192,521,596</u>	

The notes to the financial statements are an integral part of this statement.

Debt Service Fund	Capital Projects Fund	Total Non-Major Governmental Funds (See Exhibit 9)	Total Governmental Funds
\$ -	\$ -	\$32,406,172	\$ 193,564,178
180,304	464,025	55,803	1,693,373
-	-	3,272,786	119,591,406
-	-	-	60,057,262
-	-	3,969,986	5,586,168
-	-	1,792,296	14,118,717
-	-	7,844,549	40,074,217
-	-	40,552	40,552
-	-	-	5,231,165
-	-	-	20,000,000
-	-	-	8,134,859
<u>2,107,905</u>	<u>132,157,139</u>	<u>16,889,526</u>	<u>608,025,589</u>
<u>\$ 2,288,209</u>	<u>\$ 132,621,164</u>	<u>\$66,271,670</u>	<u>\$ 1,076,117,486</u>
\$ -	\$ -	\$ -	\$ 6,760,533
-	-	177,946	9,463,248
-	-	7,097,267	86,860,821
-	-	-	124,162,666
-	-	4,024,522	127,738,437
-	-	6,206,377	7,967,765
-	-	-	1,042,655
-	-	3,969,986	5,586,168
-	-	-	169,472,724
-	-	<u>21,476,098</u>	<u>539,055,017</u>
-	-	-	5,231,165
-	-	-	20,000,000
2,288,209	-	85	2,288,294
-	132,621,164	11,447,694	419,072,592
-	-	-	57,122,625
-	-	<u>33,347,793</u>	<u>33,347,793</u>
<u>2,288,209</u>	<u>132,621,164</u>	<u>44,795,572</u>	<u>537,062,469</u>
<u>\$ 2,288,209</u>	<u>\$ 132,621,164</u>	<u>\$66,271,670</u>	<u>\$ 1,076,117,486</u>

Arizona Department of Transportation
 Reconciliation of the Balance Sheet of Governmental Funds
 to the Statement of Net Assets
 June 30, 2005

Total fund balances - governmental funds (Exhibit 3) \$ 537,062,469

Amounts reported for governmental activities in the Statement of Net

Assets (Exhibit 1) are different because:

Capital assets used in governmental activities are not financial resources
 and, therefore, are not reported in the funds (Note 4 B). 12,603,336,546

Internal service funds are used by management to charge the costs
 of equipment rentals to individual funds. The assets and liabilities of
 the internal service funds are included in governmental activities in
 the Statement of Net Assets (Exhibit 5). 45,992,420

Other long-term assets are not available to pay for current-period
 expenditures and therefore are deferred in the funds (Note 4 B). 5,586,168

Long-term liabilities, including bonds payable, are not due and
 payable in the current period and, therefore, are not reported in
 the funds (Note 4 B). <1,684,960,830>

Net assets of governmental activities (Exhibit 1) \$ 11,507,016,773

The notes to the financial statements are an integral part of this statement.

Arizona Department of Transportation
Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
For the fiscal year ended June 30, 2005

		Special Revenue Funds		
		Maricopa	Motor	
		Regional	Vehicle	Highway
	General	Area Road	Division	User
	Fund	Construction	Clearing	Revenue
	(State Highway Fund)	Fund	Fund	Fund
Revenues:				
Transportation excise taxes	\$ -	\$ 316,805,562	\$ -	\$ -
Vehicle registration, title, license and related taxes and fees	149,734,911	-	656,402,577	261,768,302
Fuel and motor carrier taxes and fees	333,348,462	-	6,765,394	386,226,374
Reimbursement of construction expenditures - federal aid	392,940,136	369,327	-	-
Other federal grants and reimbursements	9,077,434	-	-	-
Reimbursements from Arizona counties and cities	15,351,798	12,074,050	-	-
Distributions from other state agencies	2,349,307	-	-	-
Interest on loans receivable	588,892	131,880	-	-
Interest on investments	7,286,612	3,447,724	-	983,892
Flight property taxes	-	-	-	-
Grand Canyon National Park Airport	-	-	-	-
Sale of capital assets	5,349,227	13,042,396	-	-
Rental income	1,120,194	475,952	-	-
Other	3,578,022	-	-	2,070,677
Total revenues	920,724,995	346,346,891	663,167,971	651,049,245
Expenditures:				
Current:				
Transportation - appropriated by				
State legislature:				
Administration	40,599,096	-	-	-
Aeronautics	-	-	-	-
Highway	63,743,830	-	-	-
Highway maintenance	105,887,007	-	-	-
Motor Vehicle	86,368,195	-	-	-
Other	169,811	-	-	-
Total Transportation - appropriated by State legislature	296,767,939	-	-	-

The notes to the financial statements are an integral part of this statement.

Debt Service Fund	Capital Projects Fund	Total Non-Major Governmental Funds (See Exhibit 10)	Total Governmental Funds
\$ -	\$ -	\$ -	\$ 316,805,562
-	-	12,484,918	1,080,390,708
-	-	33,292,602	759,632,832
-	-	110,336,935	503,646,398
-	-	-	9,077,434
-	-	4,760,310	32,186,158
-	-	-	2,349,307
-	-	224,712	945,484
3,362,360	3,700,933	380,109	19,161,630
-	-	13,180,039	13,180,039
-	-	919,327	919,327
-	-	-	18,391,623
-	-	-	1,596,146
-	-	567,168	6,215,867
<u>3,362,360</u>	<u>3,700,933</u>	<u>176,146,120</u>	<u>2,764,498,515</u>
-	-	-	40,599,096
-	-	9,516,884	9,516,884
-	-	42,440,134	106,183,964
-	-	-	105,887,007
-	-	3,839,933	90,208,128
<u>115,783</u>	<u>-</u>	<u>1,515,929</u>	<u>1,801,523</u>
<u>115,783</u>	<u>-</u>	<u>57,312,880</u>	<u>354,196,602</u>

(continued)

Arizona Department of Transportation
Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
For the fiscal year ended June 30, 2005

	General Fund (State Highway Fund)	Special Revenue Funds		
		Maricopa Regional Area Road Construction Fund	Motor Vehicle Division Clearing Fund	Highway User Revenue Fund
Distributions to Arizona counties and cities	\$ -	\$ 7,713,366	\$484,762,866	\$ 589,075,086
Distributions to other state agencies	34,693,490	-	178,405,105	61,974,159
Interest on notes payable	2,514,145	-	-	-
Debt service:				
Principal	311,866	-	-	-
Interest	8,496	-	-	-
Bond issuance costs	-	-	-	-
Non-capital, including asset preservation	178,512,763	682,017	-	-
Capital outlay	299,901,187	87,521,382	-	-
Total expenditures	<u>812,709,886</u>	<u>95,916,765</u>	<u>663,167,971</u>	<u>651,049,245</u>
Excess <deficiency> of revenues over <under> expenditures	108,015,109	250,430,126	-	-
Other financing sources <uses>:				
Transfers in	13,840,817	17,787	-	-
Transfers out for debt service	<104,473,980>	<204,938,070>	-	-
Transfers out other	<43,812>	<7,730,044>	-	-
Insurance recovery	1,518,029	-	-	-
Debt issuance	-	-	-	-
Capital leases	311,866	-	-	-
Premium from debt issuance	-	-	-	-
Total other financing sources <uses>	<u><88,847,080></u>	<u><212,650,327></u>	<u>-</u>	<u>-</u>
Net change in fund balances	19,168,029	37,779,799	-	-
Fund balances - July 1	204,374,102	96,035,594	-	-
Fund balances - June 30	<u>\$ 223,542,131</u>	<u>\$ 133,815,393</u>	<u>\$ -</u>	<u>\$ -</u>

The notes to the financial statements are an integral part of this statement.

Debt Service Fund	Capital Projects Fund	Total Non-Major Governmental Funds (See Exhibit 10)	Total Governmental Funds
\$ -	\$ -	\$ 5,403,813	\$ 1,086,955,131
-	-	31,779,763	306,852,517
-	-	-	2,514,145
301,890,000	-	-	302,201,866
91,821,897	-	-	91,830,393
-	1,996,384	-	1,996,384
-	30,530,861	176,021	209,901,662
-	236,406,122	-	623,828,691
<u>393,827,680</u>	<u>268,933,367</u>	<u>94,672,477</u>	<u>2,980,277,391</u>
<390,465,320>	<265,232,434>	81,473,643	<215,778,876>
374,161,732	-	26,025	388,046,361
-	<939,265>	<63,810,417>	<374,161,732>
-	<6,016,817>	<93,956>	<13,884,629>
-	-	-	1,518,029
-	292,645,000	-	292,645,000
-	-	-	311,866
-	24,414,008	-	24,414,008
<u>374,161,732</u>	<u>310,102,926</u>	<u><63,878,348></u>	<u>318,888,903</u>
<16,303,588>	44,870,492	17,595,295	103,110,027
18,591,797	87,750,672	27,200,277	433,952,442
<u>\$ 2,288,209</u>	<u>\$ 132,621,164</u>	<u>\$ 44,795,572</u>	<u>\$ 537,062,469</u>

Arizona Department of Transportation
 Reconciliation of the Statement of Revenues,
 Expenditures, and Changes in Fund Balances of Governmental Funds
 to the Statement of Activities
 For the fiscal year ended June 30, 2005

Net change in fund balance - total governmental funds (Exhibit 4) **\$ 103,110,027**

Amounts reported for governmental activities in the Statement of Activities (Exhibit 2)
 are different because:

Capital outlays are reported as expenditures in governmental funds (Note 4 C).	616,226,841
Bond proceeds provide current financial resources to governmental funds.	
However, issuing debt increases long-term liabilities in the statement of net assets. Governmental funds report the effect of issuance costs, premiums, discounts, and similar items when the debt is first issued, whereas these amounts are deferred and amortized in the statement of activities (Note 4 C).	<317,059,008>
Repayment of long-term debt is reported as an expenditure in governmental funds, but the repayment reduces long-term liabilities in the statement of net assets (Note 4 C).	311,360,744
Internal service funds are used by management to charge the cost of equipment rentals to individual funds. The net loss of the internal service funds is reported with governmental activities (Note 4 C).	3,857,104
Some items reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds (Note 4 C).	<u><6,506,364></u>

Change in net assets of governmental activities (Exhibit 2) **\$ 710,989,344**

The notes to the financial statements are an integral part of this statement.

PROPRIETARY FUND FINANCIAL STATEMENTS

MAJOR FUNDS

Arizona Highways Magazine Fund

The Department uses this fund in the publishing and marketing of the Arizona Highways Magazine and various other products that promote the State of Arizona.

Highway Expansion And Extension Loan Program Fund

This fund is an innovative financing mechanism to administer funds designated to provide loan and credit enhancement assistance to the Department and to sponsors of local transportation projects.

NON-MAJOR FUND

Internal Service Fund

The Department's own internal service fund, known as the Equipment Fund, purchases and maintains equipment and materials to be used by other funds and state agencies.

Arizona Department of Transportation
Statement of Net Assets
Proprietary Funds
June 30, 2005

	Business-type Activities - Enterprise Funds			Governmental
	Highway Expansion and Extension Loan Program Fund	Arizona Highways Magazine Fund	Total	Activities - Internal Service Fund
ASSETS				
Current assets:				
Unrestricted cash on deposit with the State Treasurer	\$ -	\$ 1,774,165	\$ 1,774,165	\$ 3,561,331
Restricted cash on deposit with the State Treasurer	95,305,084	-	95,305,084	-
Receivables:				
Subscriptions, net of allowance for doubtful accounts	-	396,137	396,137	-
Accrued interest	272,427	5,201	277,628	11,047
Loans	16,533,685	-	16,533,685	-
Other, net allowance for doubtful accounts	-	59,907	59,907	-
Interfund receivables (Note 5E)	4,531,210	43,815	4,575,025	-
Due from Arizona counties and cities	203,158	-	203,158	-
Inventories	-	1,137,120	1,137,120	2,797,091
Prepaid items	-	218,478	218,478	-
Total current assets	<u>116,845,564</u>	<u>3,634,823</u>	<u>120,480,387</u>	<u>6,369,469</u>
Noncurrent assets:				
Prepaid items	-	72,500	72,500	-
Loans receivable	114,896,628	-	114,896,628	-
Capital assets not subject to depreciation	-	7,900	7,900	-
Capital assets subject to depreciation, net of accumulated depreciation	-	491,574	491,574	46,668,415
Total noncurrent assets	<u>114,896,628</u>	<u>571,974</u>	<u>115,468,602</u>	<u>46,668,415</u>
Total assets	<u>231,742,192</u>	<u>4,206,797</u>	<u>235,948,989</u>	<u>53,037,884</u>
LIABILITIES				
Current liabilities:				
Accounts payable	-	112,644	112,644	149,332
Accrued payroll and other accrued expenses	4,310	106,515	110,825	417,110
Interfund payables (Note 5 E)	-	3,765	3,765	-
Compensated absences	10,120	123,402	133,522	569,193
Deferred revenue	-	3,568,479	3,568,479	-
Notes payable	-	-	-	1,233,944
Total current liabilities	<u>14,430</u>	<u>3,914,805</u>	<u>3,929,235</u>	<u>2,369,579</u>
Noncurrent liabilities:				
Advance from other funds	20,000,000	-	20,000,000	-
Notes payable	<u>146,454,466</u>	<u>-</u>	<u>146,454,466</u>	<u>4,675,885</u>
Total noncurrent liabilities	<u>166,454,466</u>	<u>-</u>	<u>166,454,466</u>	<u>4,675,885</u>
Total liabilities	<u>166,468,896</u>	<u>3,914,805</u>	<u>170,383,701</u>	<u>7,045,464</u>
NET ASSETS				
Invested in capital assets, net of related debt	-	499,474	499,474	40,758,586
Restricted for loans and other financial assistance	65,273,296	-	65,273,296	-
Unrestricted	-	<207,482>	<207,482>	5,233,834
Total net assets	<u>\$ 65,273,296</u>	<u>\$ 291,992</u>	<u>65,565,288</u>	<u>\$ 45,992,420</u>
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds			<u>3,449</u>	
Net assets of business-type activities			<u>\$ 65,568,737</u>	

The notes to the financial statements are an integral part of this statement.

Arizona Department of Transportation
Statement of Revenues, Expenses, and
Changes in Fund Net Assets
Proprietary Funds
For the fiscal year ended June 30, 2005

	Business-type Activities - Enterprise Funds			Governmental
	Highway Expansion and Extension Loan Program Fund	Arizona Highways Magazine Fund	Total	Activities - Internal Service Fund
Operating revenues:				
Sales and charges for services (net of write off \$114,314)	\$ -	\$ 8,443,339	\$ 8,443,339	\$ 34,291,452
Interest on loans receivables	3,008,667	-	3,008,667	-
Other	-	380,488	380,488	2,885,503
Total operating revenues	<u>3,008,667</u>	<u>8,823,827</u>	<u>11,832,494</u>	<u>37,176,955</u>
Operating expenses:				
Publication and promotional cost	-	4,717,154	4,717,154	-
Repair and maintenance	-	97,816	97,816	6,324,112
Fuel and lubricants	-	-	-	6,046,460
Salaries and related benefits	201,557	2,688,529	2,890,086	11,788,437
Shipping and postage	-	1,404,533	1,404,533	-
Supplies	877	96,885	97,762	335,586
Equipment purchase and rental	-	43,690	43,690	76,952
Professional and outside services	110,301	680,529	790,830	318,384
Insurance	-	-	-	605,300
Travel	1,297	9,657	10,954	83,547
Interest on notes payable	4,040,000	-	4,040,000	46,767
Depreciation	-	313,693	313,693	6,813,082
Other	5,700	220,266	225,966	961,880
Total operating expenses	<u>4,359,732</u>	<u>10,272,752</u>	<u>14,632,484</u>	<u>33,400,507</u>
Operating <loss> gain	<1,351,065>	<1,448,925>	<2,799,990>	3,776,448
Non-operating revenues <expenses>:				
Interest on investments	2,724,486	39,851	2,764,337	83,611
Loss on sale/disposal of capital assets	-	<610>	<610>	-
Total non-operating revenues <expenses>	<u>2,724,486</u>	<u>39,241</u>	<u>2,763,727</u>	<u>83,611</u>
Changes in net assets	1,373,421	<1,409,684>	<36,263>	3,860,059
Total net assets - July 1	<u>63,899,875</u>	<u>1,701,676</u>		<u>42,132,361</u>
Total net assets - June 30	<u>\$ 65,273,296</u>	<u>\$ 291,992</u>		<u>\$ 45,992,420</u>
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds			2,955	
Change in net assets of business-type activities			<u>\$ <33,308></u>	

The notes to the financial statements are an integral part of this statement.

Arizona Department of Transportation
Statement of Cash Flows
Proprietary Funds
For the fiscal year ended June 30, 2005

	Business-type Activities - Enterprise Funds			Governmental Activities - Internal Service Fund
	Highway Expansion and Extension Loan Program Fund	Arizona Highways Magazine Fund	Total	
Cash flows from operating activities:				
Receipts from customers	\$ 1,546,603	\$ 8,194,651	\$ 9,741,254	\$ -
Receipts from other funds	44,258,248	-	44,258,248	28,727,946
Receipts from other agencies	10,233,117	-	10,233,117	5,563,506
Payments to suppliers	<29,649>	<5,755,551>	<5,785,200>	<15,061,372>
Payments to employees	<214,780>	<2,676,792>	<2,891,572>	<11,815,465>
Payments to other funds	<47,427,545>	<40,050>	<47,467,595>	-
Payments to other agencies	<7,681,528>	-	<7,681,528>	-
Other receipts <payments>	<5,700>	379,533	373,833	2,875,566
Net cash provided by operating activities	<u>678,766</u>	<u>101,791</u>	<u>780,557</u>	<u>10,290,181</u>
Cash flows from capital and related financing activities:				
Proceeds from sale of capital assets	-	-	-	591,004
Acquisition of capital assets	-	<3,765>	<3,765>	<9,386,753>
Net cash <used in> capital and related financing activities	-	<3,765>	<3,765>	<8,795,749>
Cash flows from investing activities:				
Interest on investments	<u>2,587,637</u>	<u>39,851</u>	<u>2,627,488</u>	<u>83,611</u>
Net cash provided by investing activities	<u>2,587,637</u>	<u>39,851</u>	<u>2,627,488</u>	<u>83,611</u>
Net increase in cash	3,266,403	137,877	3,404,280	1,578,043
Cash - July 1	<u>92,038,681</u>	<u>1,636,288</u>	<u>93,674,969</u>	<u>1,983,288</u>
Cash - June 30	<u>\$ 95,305,084</u>	<u>\$ 1,774,165</u>	<u>\$ 97,079,249</u>	<u>\$ 3,561,331</u>
Reconciliation of operating <loss> gain to net cash provided by operating activities:				
Operating <loss> gain	\$ <1,351,065>	\$ <1,448,925>	\$ <2,799,990>	\$ 3,776,448
Adjustment to reconcile operating <loss> gain to net cash provided by operating activities:				
Depreciation	-	313,693	313,693	6,813,082
Net changes in assets and liabilities:				
Receivables	<536,179>	84,787	<451,392>	<9,937>
Due from other Arizona Department of Transportation funds	<1,645,053>	<40,050>	<1,685,103>	-
Due from Arizona counties and cities	182,989	-	182,989	-
Inventories	-	1,136,815	1,136,815	<294,663>
Prepaid items	-	394,210	394,210	-
Accounts payable	-	<16,046>	<16,046>	<51,268>
Accrued payroll and other accrued expenses	<2,401>	19,905	17,504	60,624
Compensated absences	<9,525>	<8,168>	<17,693>	<4,105>
Notes payable	4,040,000	-	4,040,000	-
Deferred revenue	-	<334,430>	<334,430>	-
Net cash provided by operating activities	<u>\$ 678,766</u>	<u>\$ 101,791</u>	<u>\$ 780,557</u>	<u>\$ 10,290,181</u>

The notes to the financial statements are an integral part of this statement.

FIDUCIARY FUND FINANCIAL STATEMENT

AGENCY FUNDS

Highway Properties - Privilege Tax Fund

This fund collects monies from renters of properties previously acquired by the Department for use in future highway development. Monies collected are distributed to the Department of Revenue.

Highway Properties - 24% Lieu Tax Fund

This fund collects 24 percent of the Department's rental income from properties for use in future highway development. Monies collected are distributed to the local counties.

Arizona Department of Transportation
Statement of Net Assets
Agency Funds
June 30, 2005

ASSETS

Restricted cash on deposit with the State Treasurer	\$ 248,415
Total assets	<u>\$ 248,415</u>

LIABILITIES

Due to Department of Revenue	\$ 220
Due to Arizona counties	<u>248,195</u>
Total liabilities	<u>\$ 248,415</u>

The notes to the financial statements are an integral part of this statement.

Notes to the Financial Statements

Arizona Department of Transportation
Comprehensive Annual Financial Report
For the Fiscal Year Ended June 30, 2005

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1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Arizona Department of Transportation (Department) conform in all material respects to accounting principles generally accepted in the United States of America (GAAP) as applicable to governments. The Governmental Accounting Standards Board (GASB) is the primary standard setting body for establishing governmental accounting and financial reporting principles, which are primarily set forth in the GASB's *Codification of Governmental and Financial Reporting Standards* (GASB Codification). Following is a summary of the Department's significant accounting policies.

A. Reporting Entity

The Department is a department of the State of Arizona (State) and is not a legally separate entity. The Department has no component units. The Director of the Department serves as the Chief Administrative Officer and is directly responsible to the Governor. The Governor appoints a seven-member Transportation Board of the State of Arizona Department of Transportation (Transportation Board) which has responsibility for establishing a complete system of state highway routes, approving all highway construction contracts, and distributing monies for local airport facilities' projects through a grant program.

The Department is responsible for the construction and maintenance of all state highways. The Department cooperates with the various cities and counties within the state in the construction and maintenance of state roads and with the Federal Highway Administration in the construction and maintenance of interstate and other highways. Assistance in the development of local airports, registering motor vehicles and aircraft, licensing drivers and the publishing of the *Arizona Highways Magazine* are also responsibilities of the Department.

B. Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the government. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by federal reimbursement, taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for services.

The **Statement of Net Assets** presents the reporting entity's non-fiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.

Restricted net assets result when constraints placed on asset use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources which are imposed by management, but can be removed or modified by management or the Transportation Board.

The **Statement of Activities** demonstrates the degree to which the direct expenses of a given function are offset by program revenues. *Direct expenses* are those that are clearly identified with a specific function. *Program revenues* include: 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services or privileges provided by a given function and 2) grants and contributions that are restricted to meeting the operational or capital

Arizona Department of Transportation
Notes to the Financial Statements
June 30, 2005

requirements of a particular function. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Fund Financial Statements

Separate statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major proprietary funds are reported as separate columns in the fund financial statements, with non-major funds being reported in a single column.

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the *economic resources measurement focus* and the full *accrual basis of accounting*, as are the proprietary funds. Revenues are recorded when earned and expenses are recorded when the liability is incurred, regardless of the timing of related cash flows. Taxes are recognized as revenues in the year they are levied for transportation excise, aircraft licensing, aviation and motor fuel, flight property, and underground storage tanks. Motor carrier and vehicle license taxes are recognized when received. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

As allowed by GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the Department's enterprise funds follow GASB pronouncements and those Financial Accounting Standard Board Statements (FASB) and Interpretations, Accounting Principle Board Opinions, and Accounting Research Bulletins that were issued on or before November 30, 1989, except those that conflict with a GASB pronouncement. The enterprise funds do not follow any FASB Statements and Interpretations issued after November 30, 1989.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Department considers revenues to be available if they are collected within 60 days of the end of the fiscal year, e.g. federal revenue reimbursements, vehicle license taxes and highway user revenue taxes. Expenditures generally are recorded when a liability is incurred as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due and payable.

Financial Statement Presentation

The Department reports the following major governmental funds:

The *General Fund*, known as the State Highway Fund, is the primary operating fund. It accounts for all financial resources except for those required to be accounted for in another fund. Expenditures are reported for general operations of the Department, including road and bridge repairs, maintenance and construction, planning and development, engineering, and administration. Revenues are received from the following primary sources: fuel and motor carrier taxes and fees; vehicle registrations, titles, licenses and related fees; and federal grants.

The *Maricopa Regional Area Road Construction Fund* is a special revenue fund that receives Maricopa County transportation excise tax monies collected by the Department of Revenue. These monies are used for the construction of certain state highways within Maricopa County.

The *Motor Vehicle Division Clearing Fund* is a special revenue fund, which accounts for the collection and disbursement of certain Motor Vehicle Division revenues.

Arizona Department of Transportation
Notes to the Financial Statements
June 30, 2005

The *Highway User Revenue Fund* is a special revenue fund, which collects motor vehicle and liquid use fuel taxes and receives certain Motor Vehicle Division revenues from the Motor Vehicle Division Clearing Fund. These monies are distributed to the State Highway Fund, the Department of Public Safety, the Arizona State Parks, the Economic Strength Project Fund, and incorporated cities and counties.

The *Debt Service Fund* is used to account for the accumulation of resources for, and the payments of, general long-term debt principal and interest of the governmental funds.

The *Capital Projects Fund* is used to account for financial resources to be used for the acquisition or construction of major capital facilities of the governmental funds.

The Department reports the following major proprietary funds:

The *Highway Expansion and Extension Loan Program Fund* (HELP) is an innovative financing mechanism to administer funds designated to provide loan and credit enhancement assistance to sponsors of local transportation projects.

The *Arizona Highways Magazine Fund* publishes and markets the Arizona Highways Magazine and various other products that promote the State of Arizona.

Additionally, the Department reports the following fund types:

The *Internal Service Fund*, which accounts for purchases and maintenance of equipment and materials to be used by other divisions in the Department and other government agencies. The Equipment Fund is the Department's only internal service fund.

The *Agency Funds* are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. The Department has two agency funds, the Highway Properties – Privilege Tax and the Highway Properties – 24% Lieu Tax (neither are included in the government-wide statements).

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges for services by the Equipment Fund to the other governmental functions. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as *program revenues* include: 1) charges for services, 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as *general revenues* rather than program revenues. Likewise, general revenues include all taxes.

Proprietary funds distinguish *operating* revenues and expenses from *non-operating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues are charges for services and magazine subscriptions. The Department also recognizes as operating revenues interest on loan receivables and other revenues intended to recover the cost of services. Operating expenses for the enterprise funds and the internal service fund include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

When both restricted and unrestricted resources are available for use, the Department generally expends the restricted resources first, and then unrestricted resources, as they are needed to maintain appropriate cash balances and finance the construction program.

D. Assets, Liabilities, and Net Assets/Fund Balance

Deposits and Investments

The Department's cash includes petty cash, bank accounts, and deposits with the State Treasurer for pooled investments. All investments are carried in the name of the State of Arizona. State statutes require the State Treasurer to invest these pooled funds in collateralized time certificates of deposit, repurchase agreements or obligations of the U.S. Government. All investments are carried at fair value. These balances are not subject to GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*, classification because they are included in the state's investment pool. As of June 30, 2005, the state's investment pools were not rated.

State statutes require the State Treasurer to maintain separate investment accounts for the portions of the Highway Revenue Bond Proceeds Fund relating to the highway revenue bond issues and the Maricopa Regional Area Road Bond Proceeds Fund relating to the transportation excise tax revenue bond issues. These funds may be invested by the Treasurer in the state's investment pool.

The Department's investments are included in the state investment pool and these investments are not shown in the Department's name. Therefore, the Department presents its equity in the internal pool as required in GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*.

The Department has restricted cash for payment of capital projects for Maricopa and Pima counties, for future debt service payments, and for loan repayment to the HELP fund.

Receivables, Payables and Advances

Activities between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as interfund receivables/payables. All other outstanding balances between U.S. Government, Arizona counties and cities, and other state agencies are reported as "due to/from". Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances".

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

The other receivables and subscriptions receivables are shown net of allowance for doubtful accounts. Other receivables in excess of 180 days comprise the recoverable insurance claims net of allowance for doubtful accounts. The subscriptions receivable allowance for doubtful accounts is equal to outstanding subscription payments past due more than 90 days.

Notes receivable represents real estate mortgage loans made to individuals purchasing homes previously owned by the Department for highway construction purposes. The loans were made at a fixed rate and mature ten years from the date of origination.

Inventories and Prepaid Items

The governmental activities inventory is valued at cost, which approximates market, using the moving average method. This inventory is accounted for using the consumption method. Under this method, inventories are recorded as expenditures as they are used. The fund financial statement shows a reservation for inventory for the like amount

Arizona Department of Transportation
Notes to the Financial Statements
June 30, 2005

indicating it does not constitute available expendable resources. No reservation of net assets is shown in the government-wide statements for inventories.

The business-type activities' inventories are stated at the lower of cost or market. Costs of enterprise fund inventories consisting of resale products and supplies are generally determined by moving average cost and specific identification methods, respectively. Costs of the internal service fund's inventories (consisting of vehicle parts and supplies, fuels and lubricants, and other supplies) are determined by moving average cost methods.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements.

Restricted Assets

Certain proceeds of the Department's governmental revenue bonds, as well as certain resources of the General Fund and the Highway Expansion and Extension Loan Program Fund (enterprise fund) are classified as restricted assets on the balance sheet because they are maintained in separate bank accounts and their use is limited by applicable bond covenants or state statutes. Effective July 1, 1981, state law required accumulation of at least 15 percent, which in fiscal year 1996 was modified to 12.6 percent, of the revenues allocated each year to the General Fund (State Highway Fund) from the Highway User Revenue Fund for the design, purchase of right-of-way or construction of controlled-access highways which are included in the regional transportation plan of counties with populations in excess of 400,000 (Maricopa and Pima counties). The debt service fund is used to report the resources set aside for payment of future debt service. Bond proceeds are deposited in the capital projects fund and are restricted for acquisitions of right-of-way and construction of federal, state and local highways.

The Department has restricted cash for payment of capital projects for Maricopa and Pima counties, for future debt service payments, and for loan repayment to the HELP fund.

Capital Assets

Capital assets, which include land, buildings and improvements, improvements other than buildings, machinery and equipment, infrastructure and construction in progress, are reported in the applicable governmental or business-type columns in the government-wide financial statements. Capital assets are defined by the Department as assets with an initial, individual cost of \$5,000 or more and an estimated useful life in excess of one year. Purchased capital assets are recorded at historical cost or estimated historical cost if historical cost is not available. Donated capital assets are recorded at estimated fair value at the date of donation.

Costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the assets' lives are not capitalized. Outlays for capital assets are capitalized at the time of the purchase or, in the case of infrastructure, at the time of final acceptance by the Department from the contractor. Asset preservation costs are expensed as incurred.

The Department depreciates non-infrastructure capital assets on a straight-line basis using the following estimated useful lives. Modular buildings are included on the Statement of Net Assets under the machinery and equipment category; however, modular buildings have an estimated useful life of fifteen (15) years.

Assets	Years
Buildings and improvements	40
Improvements other than building	40
Machinery and equipment	5-15
Mobile fleet and aircraft	5-15

Arizona Department of Transportation
Notes to the Financial Statements
June 30, 2005

Infrastructure was capitalized for the first time in fiscal year 2002. The infrastructure assets are reported in the governmental-type activities column of the Statement of Net Assets. The Department's infrastructure assets consist of roads and bridges and are presented using the modified approach and, therefore, are not depreciated.

In order to utilize the modified approach, the Department is required to: 1) maintain an asset management system that includes an up to date inventory of eligible infrastructure assets, 2) perform condition assessments of eligible assets and summarize the results using a measurement scale, 3) estimate each year the annual amount to maintain and preserve the assets at the condition level established and disclosed by the Department, and 4) document that the assets are being preserved approximately at or above the established condition level.

Deferred Revenues

In the government-wide statements and proprietary fund financial statements, deferred revenues are recognized when cash, receivables, or other assets are received prior to being recognized. In the governmental funds, amounts are reported as deferred revenues until they are available to liquidate liabilities of the current period. Deferred revenues are reported in the government-wide statements for the business-type activities and in the fund statements for both the governmental and proprietary funds. In the government-wide statements, the deferred revenues relate to unearned subscription revenue for the *Arizona Highways Magazine*. Unearned subscription revenue is recorded when subscription orders are received and is amortized as revenue over the terms of the related subscriptions. Costs associated with the selling of subscriptions are expensed in the year incurred. In the fund statements, the deferred revenue represents the amount for the notes receivable for real estate mortgage loans made to individuals who purchased homes previously owned by the Department for highway construction purposes. The loans were made at a fixed rate and mature ten years from the date of origination.

Compensated Absences

It is the Department's policy to permit employees to accumulate earned but unused sick leave and vacation benefits as well as compensatory time. There is no liability for unpaid accumulated sick leave for the Department. All vacation pay and compensatory time is accrued when incurred in the government-wide and proprietary fund financial statements.

Effective July 1, 1998, state employees are eligible to receive payment for an accumulated sick leave balance of 500 hours or more with a maximum of 1,500 hours, upon retirement directly from state service. The benefit value is calculated by taking the state hourly rate of pay at the retirement date, multiplied by the number of sick hours at the retirement date, times the eligibility percentage. The eligibility percentage varies based upon the number of accumulated sick hours from 25 percent for 500 hours to a maximum of 50 percent for 1,500 hours. The maximum benefit value is \$30,000. The benefit is paid out in annual installments over three years. The Retiree Accumulated Sick Leave Fund is accounted for on the State's financial statements as an Internal Service Fund.

Employees are allowed to accumulate up to 240 hours of vacation leave (320 hours for uncovered employees) and up to 240 hours of compensatory time which is paid when vacation or compensatory time is taken or upon termination of employment at the individual's then current rate of pay. The liabilities for vacation and compensatory time outstanding as of June 30 for both the governmental and proprietary funds are reported on the Statement of Net Assets.

Long-term Obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method, which approximates the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

Arizona Department of Transportation
Notes to the Financial Statements
June 30, 2005

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as issuance costs, during the current period. The face amount of the debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Net Assets/Fund Balance

The difference between assets and liabilities is “Net Assets” on the government-wide and proprietary statements and “Fund Balance” on the governmental fund statements.

Reservations

Fund balances for governmental funds are classified as either reserved or unreserved in the fund financial statements. Reserved fund balances reflect either: 1) funds legally segregated for a specific purpose, or 2) assets, which by their nature, are not available for expenditure. Unreserved fund balances reflect the balances available for appropriation for the general purposes of the fund.

E. Revenues and Expenditures/Expenses

In the government-wide Statement of Activities, revenues and expenses are segregated by activity (governmental or business-type), then further by function (e.g. Administration, Aeronautics, Highway, etc). Additionally, revenues are classified between program and general revenues. Program revenues include: 1) charges for services, 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as general revenue rather than as program revenue. General revenue includes all taxes and interest on investments.

In the governmental fund financial statements, revenues are reported by source. Expenditures are reported by function (e.g., Administration, Distributions to Arizona counties and cities, and Distributions to other state agencies, Debt service, Capital outlay, etc.).

The Distributions to Arizona counties and cities and Distributions to other state agencies are shared tax revenues that are distributed based on statutory requirements. Debt service includes both interest and principal outlays related to bonds. Capital outlay includes expenditures for real property or infrastructure (e.g. bridges and roads).

Revenues and expenses of proprietary funds are classified as operating and non-operating and are sub-classified by object (e.g., salaries, equipment rental, depreciation, etc). Operating revenues and expenses generally result from providing services and producing and delivering goods. All other revenues and expenses are reported as non-operating.

Other Financing Sources <Uses>

Other financing sources are additions to the governmental fund balances in the fund financial statements and include resources and financing provided by bond proceeds, capital leases, insurance recovery and transfers from other funds. Other financing uses are reductions of governmental fund resources in fund financial statements normally resulting from transfers to other funds.

F. Interfund Activity and Balances

Interfund Activity

As a general rule, the effect of interfund activity has been eliminated from the government-wide statements. Exceptions to this rule are activities between the funds reported as governmental activities and the funds reported as business-type activities (e.g. the transfer of the gain or loss from the Equipment Fund).

Arizona Department of Transportation
Notes to the Financial Statements
June 30, 2005

Interfund Balances

Interfund receivables and payables have been eliminated from the Statement of Net Assets, except for the residual amounts due between governmental and business-type activities.

2. FUNDS BY CLASSIFICATION

The following table lists all of the funds whose balances are reflected in this financial report.

MAJOR FUNDS

Governmental Funds :

General Fund (State Highway Fund)

Special Revenue Funds:

Maricopa Regional Area Road

Construction Fund

Motor Vehicle Division Clearing Fund

Highway User Revenue Fund

Debt Service Fund

Capital Projects Fund

Proprietary Funds:

Arizona Highways Magazine Fund

Highway Expansion and Extension

Loan Program Fund

FIDUCIARY FUNDS

Agency Funds:

Highway Properties - Privilege Tax Fund

Highway Properties - 24% Lieu Tax Fund

NON-MAJOR FUNDS

Other Governmental Funds:

Special Revenue Funds:

State Aviation Fund

Safety Enforcement and Transportation

Infrastructure Fund

Motor Vehicle Liability Insurance

Enforcement Fund

Vehicle Inspection and Title

Enforcement Fund

Grant Anticipation Notes Fund

Local Agency Deposits Fund

Motorcycle Safety Education Fund

Underground Storage Tank Fund

Economic Strength Project Fund

3. BUDGETING, BUDGETARY CONTROL, AND LEGAL COMPLIANCE

Annual budgets for the operating expenditures and capital outlay including land, building and improvements for the General Fund (State Highway Fund) are submitted to the Governor in accordance with state law. The budgets are legally enacted as appropriations after approval by the state legislature and signature by the Governor. The legal level of control for operating expenditures is at the program level and expenditure budgets are appropriated using a lump sum format with special line items. Expenditure details for personal services, employee related expenditures and all other operating expenditures are specifically budgeted within all divisions. In certain divisions, other specific programs are budgeted in addition to these categories. Revenue budgets are developed internally by the Department and are not a part of the appropriation process.

Amendments to the approved appropriations require legislative approval. However, since the Department's appropriation is a lump sum appropriation by program, the allocation of funds between personal services, employee-related expenses, and other operating expenditures is an internal decision for the program manager. Accordingly, transfers between line items such as personal services and other operating expenditures within a particular program may be made by the program manager. Transfers of funds between programs require the approval of the Director of the Department of Administration. Expenditures may not exceed appropriations.

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All transfers of funds are reported to the Department's Office of Strategic Planning and Budgeting for monitoring purposes.

Budgets are prepared on the cash basis except that liabilities incurred before the end of the fiscal year and paid within the first month of the subsequent fiscal year are charged against the prior fiscal year's budget. The Department's appropriations lapse at year-end unless exempted by the legislature.

The capital outlay appropriation includes state highway construction and land, buildings and improvements for the General Fund (State Highway Fund). A legal limitation is adopted for land, buildings and improvements; however, legislation allows the Department to spend in excess of its appropriation for state highway construction up to the current fund balance. The Department monitors expenditures through an internal budgetary process and the Five-Year Transportation Facilities Construction Program approved by the Transportation Board. A legal limitation is not adopted for the other special revenue funds, the debt service funds, capital projects funds, proprietary funds and fiduciary funds.

4. ACCOUNTING PRONOUNCEMENTS AND RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

A. New Accounting Pronouncements

Statement No. 40, *Deposit and Investment Risk Disclosures – an amendment to GASB Statement No. 3*

In March 2003, GASB issued Statement No. 40. This Statement addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest rate risk, this Statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. Deposit and investment policies related to the risks identified in this Statement also should be disclosed. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2004. Since all of the Department's investments are placed in the State Treasurer's investment pools, and the pools are not rated, no other provisions of this Statement are applicable to the Department.

Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other than Pension Plans*, issued April 2004.

Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefit Plans Other than Pensions*, issued June 2004.

Statement Nos. 43 and 45 relate to postemployment benefits. The Department does not offer such benefits, consequently, these Statements are not applicable to the Department.

Statement No. 44, *Economic Condition Reporting: The Statistical Section, an amendment of NCGA Statement 1*, issued May 2004

This Statement amends the portions of NCGA Statement 1, *Governmental Accounting and Financial Reporting Principles*, that guide the preparation of the statistical section. The statistical section presents detailed information, typically in ten-year trends, that assists users in utilizing the basic financial statements, notes to basic financial statements, and required supplementary information to assess the economic condition of a government. This Statement applies to any statistical section that accompanies a government's basic financial statements. The provisions of this Statement are effective for statistical sections for periods beginning after June 15, 2005. The Department has not yet implemented this Statement.

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Statement No. 46, *Net Assets Restricted by Enabling Legislation*

In December 2004, GASB issued Statement No. 46. This Statement requires that limitations on the use of net assets imposed by legislation be reported as restricted net assets. The Statement clarifies that a legally enforceable enabling legislation restriction is one that a party external to a government – such as citizens, public interest groups, or the judiciary – can compel a government to honor. This Statement also specifies the accounting and financial reporting requirements if new enabling legislation replaces existing enabling legislation or if legal enforceability is reevaluated. The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2005. The Department has not yet implemented this Statement.

Statement No. 47, *Accounting for Termination Benefits*

This Statement was issued in June 2005. The Statement requires employers to disclose a description of the termination benefit arrangement, the cost of the termination benefits (required in the period in which the employer becomes obligated if that information is not otherwise identifiable from information displayed on the face of the financial statements), and significant methods and assumptions used to determine termination benefit liabilities. The requirements of the Statement are effective for financial statements for periods beginning after June 15, 2005. Earlier application is encouraged. The Department has not yet implemented this Statement.

B. Explanations of Reconciling Items of the Balance Sheet of Governmental Funds to the Statement of Net Assets

The governmental funds balance sheet includes a reconciliation between fund balance – total governmental funds and net assets – government activities as reported on the government-wide Statement of Net Assets. The following explanations are necessary to explain these differences between the governmental fund Balance Sheet and the government-wide Statement of Net Assets:

1. Capital assets are not included on the fund statements but are included on the government-wide statement as follows:

Capital assets not subject to depreciation	\$ 12,463,022,388
Capital assets subject to depreciation	<u>186,982,573</u>
	12,650,004,961
less Internal Service Fund (Equipment Fund) assets	<46,668,415>
	<u><u>\$ 12,603,336,546</u></u>

2. Deferred revenues for assets shown in fund statements for the following funds:

General Fund (State Highway Fund)	\$ 317,372
Maricopa Regional Area Road Construction Fund	1,298,810
State Aviation Fund	<u>3,969,986</u>
	<u><u>\$ 5,586,168</u></u>

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3. Long-term liabilities, including bonds payable, are not due and payable in the current period and are not reported in the current period on the fund statements. The detail for the \$<1,684,960,831> difference is as follows:

Bonds payable	\$<1,682,421,480>
Deferred charges - bond issuance costs	6,069,876
Capital leases	311,866
Compensated absences	<8,918,138>
Business activity share of Equipment Fund gain <loss>	<u><2,955></u>
	<u>\$<1,684,960,831></u>

C. Explanations of Reconciling Items of the Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statement of Activities

The governmental funds statement of revenues, expenditures, and changes in fund balances includes a reconciliation between net changes in fund balances – total governmental funds and changes in net assets of governmental activities as reported on the government-wide Statement of Activities. The following explanations are necessary to explain these differences between the governmental fund Statement of Revenues, Expenditures, and Changes in Fund Balances and the government-wide Statement of Activities:

1. Governmental funds report capital outlay as expenditures. However, in the Statement of Activities, these costs are removed; some costs are capitalized as assets while other costs are expensed as follows:

Capital outlay	\$ 623,828,691
Less depreciation expense	<u><7,601,850></u>
	<u>\$ 616,226,841</u>

2. The issuance of long-term debt (e.g. bonds) provides current financial resources to governmental funds, while the repayment of principal of long-term debt consumes current financial resources of the governmental funds. Neither transaction, however, has any effect on net assets. Also, the government reports the effect of bond issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are amortized in the Statement of Activities. The details of this \$<5,698,264> difference are as follows:

Debt issued or incurred:	
Issuance of Highway Revenue Bonds	\$ <188,260,000>
Issuance of Grant Anticipation Notes	<104,385,000>
Premium on bonds	<u><24,414,008></u>
	<u><317,059,008></u>
Principal repayments:	
Highway Revenue Bonds	44,265,000
Transportation Excise Tax Revenue Bonds	208,625,000
Grant Anticipation Notes	49,000,000
Amortization of premium and discount	7,474,360
Amortization of bond issuance costs	<u>1,996,384</u>
	<u>311,360,744</u>
	<u>\$ <5,698,264></u>

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3. The Internal Service Fund is used by the Department to charge the cost for purchases and maintenance of equipment and material to be used by other funds and state agencies. The gain <loss> in the Internal Service Fund represents over <under>-billing and must be eliminated from the government-wide Statement of Activities for the business activity.

Internal Service Fund (Equipment Fund):

Changes in net assets	\$ 3,860,059
Business activity share of Equipment Fund <gain> loss	<2,955>
	<u>\$ 3,857,104</u>

4. Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore, are not reported as expenditures in the governmental funds. The details are as follows:

Highway administration	\$ <8,057,809>
Sales/disposals of capital assets	2,045,021
Capital lease payments	1,120,965
Notes & loans	<1,272,807>
Compensated absences	<341,734>
	<u>\$ <6,506,364></u>

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5. DETAILED NOTES ON ALL FUNDS

A. Capital Assets

Capital assets activity for the year ended June 30, 2005, was as follows:

Governmental Activities	July 1, 2004 Beginning Balance	Increases	Decreases	June 30, 2005 Ending Balance
Capital Assets, not being depreciated:				
Land	\$ 1,858,113,828	\$ 38,613,911	\$ <20,957,253>	\$ 1,875,770,486
Infrastructure	8,591,370,632	272,271,621	<14,561>	8,863,627,692
Construction in progress	<u>1,401,933,559</u>	<u>577,877,481</u>	<u><256,186,830></u>	<u>1,723,624,210</u>
Total Capital Assets, not being depreciated	<u>11,851,418,020</u>	<u>888,763,013</u>	<u><277,158,644></u>	<u>12,463,022,388</u>
Capital Assets, being depreciated:				
Buildings and improvements	145,768,717	938,765	-	146,707,482
Improvements other than buildings	34,032,364	699,892	-	34,732,256
Machinery and equipment	46,443,528	4,512,364	<2,016,568>	48,939,324
Mobile Fleet and aircraft	<u>115,814,957</u>	<u>14,768,684</u>	<u><6,117,524></u>	<u>124,466,117</u>
Total Capital Assets, being depreciated	<u>342,059,566</u>	<u>20,919,705</u>	<u><8,134,092></u>	<u>354,845,179</u>
Less accumulated depreciation for:				
Buildings and improvements	<51,792,948>	<3,009,909>	-	<54,802,857>
Improvements other than buildings	<1,881,295>	<321,061>	-	<2,202,356>
Machinery and equipment	<30,005,541>	<4,411,913>	2,103,066	<32,314,388>
Mobile Fleet and aircraft	<u><77,337,849></u>	<u><6,672,049></u>	<u>5,466,893</u>	<u><78,543,005></u>
Total accumulated depreciation	<u><161,017,633></u>	<u><14,414,932></u>	<u>7,569,959</u>	<u><167,862,606></u>
Total Capital Assets, being depreciated, net	<u>181,041,933</u>	<u>6,504,773</u>	<u><564,133></u>	<u>186,982,573</u>
Governmental activities capital assets, net	<u>\$ 12,032,459,953</u>	<u>\$ 895,267,786</u>	<u>\$ <277,722,777></u>	<u>\$ 12,650,004,961</u>

Business-Type Activities	July 1, 2004 Beginning Balance	Increases	Decreases	June 30, 2005 Ending Balance
Capital Assets, not being depreciated:				
Land	\$ 7,900	\$ -	\$ -	\$ 7,900
Capital Assets, being depreciated:				
Buildings and improvements	981,157	-	-	981,157
Machinery and equipment	<u>2,368,035</u>	<u>3,765</u>	<u><6,097></u>	<u>2,365,703</u>
Total Capital Assets, being depreciated	<u>3,349,192</u>	<u>3,765</u>	<u><6,097></u>	<u>3,346,860</u>
Less accumulated depreciation for:				
Buildings and improvements	<703,190>	<33,816>	-	<737,006>
Machinery and equipment	<1,843,891>	<279,877>	5,488	<2,118,280>
Total accumulated depreciation	<u><2,547,081></u>	<u><313,693></u>	<u>5,488</u>	<u><2,855,286></u>
Total Capital Assets, being depreciated, net	802,111	<309,928>	<609>	491,574
Business type activities capital assets, net	<u>\$ 810,011</u>	<u>\$ <309,928></u>	<u>\$ <609></u>	<u>\$ 499,474</u>

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Depreciation expense was charged to functions/programs as follows:

Governmental Activities:	
Administration	\$ 1,786,273
Aeronautics	284,669
Highway	2,471,153
Highway Maintenance	1,477,608
Motor Vehicle	1,582,147
Capital assets held by the Department's internal service fund are charged to the various functions based on their usage of the assets	<u>6,813,082</u>
Total depreciation expense - governmental activities	<u>\$ 14,414,932</u>
Business-type Activities	
Arizona Highways Magazine Fund	<u>\$ 313,693</u>

B. Construction Commitments

The Department's outstanding commitments for contracts at June 30, 2005, were \$627,447,779.

	Expenditures To Date	Remaining Commitment
Construction contracts:		
Rural roadways	\$ 253,636,947	\$ 130,114,621
Small urban roadways	26,017,594	16,311,160
Urban roadways	46,027,739	39,714,037
Large urban roadways	<u>543,350,071</u>	<u>234,256,868</u>
Sub-total	869,032,351	420,396,686
Design contracts	897,145,149	103,793,199
Other commitments	146,242,902	103,257,894
Total	<u>\$ 1,912,420,402</u>	<u>\$ 627,447,779</u>

C. Deferred Revenues

In the fund financial statements, the deferred revenues represent the amount for notes receivable for real estate mortgage loans made to individuals who purchased homes previously owned by the fund for highway construction purposes. The loans were made at a fixed rate and mature ten years from the date of origination. The State Aviation Fund amount represents loans to various local governments for construction of hangars, taxiways extension, runways, etc. These loans were made at a fixed rate and with various maturities. The proprietary fund includes the amount for unearned subscriptions. The following schedule is a summary of the amounts outstanding as of June 30, 2005:

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Governmental Funds:

General Fund (State Highway Fund)	\$ 317,372
Maricopa Regional Area Road Construction Fund	1,298,810
State Aviation Fund	3,969,986
	<u>\$ 5,586,168</u>

Proprietary Fund:

Arizona Highways Magazine Fund	<u>\$ 3,568,479</u>
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D. Securities Held in Lieu of Retention

In accordance with Arizona law, a contractor may assign to the Department securities in lieu of retention and will deposit with the bank, cash, time certificates of deposit in federally insured banks licensed by the State of Arizona (Certificates of Deposit), securities of or guaranteed by the United States of America (Treasury Bills), or other eligible securities as defined in the Arizona Revised Statutes, Title 35, Chapter 2, Article 2, Section 35-313. At June 30, 2005, the bank held assignment on securities aggregating approximately \$24 million in lieu of contractor retentions for construction. These additional securities are not reflected in the accompanying financial statements.

E. Interfund Receivables, Payables, Advances and Transfers

The balances of current interfund receivables and payables as of June 30, 2005, were:

<u>Receivables</u>	<u>Payables</u>	<u>Amount</u>
Governmental activities:		
General Fund (State Highway Fund)	Highway User Revenue Fund	\$ 97,222,524
	Arizona Highways Magazine Fund	3,765
	Maricopa Regional Area Road Fund	85,000
	Motor Vehicle Division Clearing Fund	24,686
Maricopa Regional Area Road Fund	Motor Vehicle Division Clearing Fund	20,430
Motor Vehicle Division Clearing Fund	General Fund (State Highway Fund)	742,860
Highway User Revenue Fund	Motor Vehicle Division Clearing Fund	18,036,616
	General Fund (State Highway Fund)	182,739
Non-major governmental funds	Motor Vehicle Division Clearing Fund	<u>3,272,786</u>
		<u>119,591,406</u>
Business-type activities:		
Arizona Highways Magazine Fund	General Fund (State Highway Fund)	43,815
Highway Expansion and Extension Loan Program Fund	General Fund (State Highway Fund)	<u>4,531,210</u>
		<u>4,575,025</u>
		<u>\$ 124,166,431</u>

The General Fund receivable of \$97,222,524 is an accrual for fuel tax revenues imposed in fiscal year 2005 from the Highway User Revenue Fund that will be collected in fiscal year 2006.

The Highway User Revenue Fund receivable of \$18,036,616 is an accrual for vehicle license taxes due in fiscal year 2005 from the Motor Vehicle Division Clearing Fund that will be collected in fiscal year 2006.

In a prior fiscal year, the General Fund advanced \$20 million to the Highway Expansion and Extension Loan Program Fund to increase its loan capacity. The advance is due no later than December 31, 2008.

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Interfund transfers for the year ended June 30, 2005, consisted of the following:

	Interfund Transfer In:				
	General Fund (State Highway Fund)	Maricopa Regional Area Road Construction Fund	Debt Service Fund	Non-Major Governmental Funds	Total
<u>Interfund Transfer Out:</u>					
General Fund (State Highway Fund)	\$ -	\$ 17,787	\$ 104,473,980	\$ 26,025	\$104,517,792
Capital Projects Fund	6,016,817	-	939,265	-	6,956,082
Maricopa Regional Area Road Construction Fund	7,730,044	-	204,938,070	-	212,668,114
Non-Major Governmental Funds	<u>93,956</u>	<u>-</u>	<u>63,810,417</u>	<u>-</u>	<u>63,904,373</u>
Total	<u>\$13,840,817</u>	<u>\$ 17,787</u>	<u>\$ 374,161,732</u>	<u>\$ 26,025</u>	<u>\$388,046,361</u>

The General Fund (State Highway Fund) (\$104,473,980), the Maricopa Regional Area Road Construction Fund (\$204,938,070) and Other Governmental Funds - Grant Anticipation Notes Fund (\$63,810,417) made transfers to the Debt Service Fund to pay bond debt service.

F. Leases

Operating Leases

The Department leases data processing equipment, other equipment, and certain facilities from various lessors. The majority of these leases are for a one-year term, renewable annually. Total rental expenditures (excluding interfund transactions) for the fiscal year ended June 30, 2005, approximated \$2,737,116.

In fiscal year 2002, the Department renegotiated its long-term lease with the City of Phoenix for a facility located on Washington Street in Phoenix. The future operating lease commitments are as follows:

Year ending June 30	Amount
2006	\$ 777,243
2007	818,150
Future operating lease commitments	<u>\$ 1,595,393</u>

In fiscal year 2003, the Department entered into a long-term lease to build a structure to house lab facilities in Gilbert, Arizona. The future operating lease commitments are as follows:

Year ending June 30	Amount
2006	\$ 101,820
2007	101,820
2008	105,489
2009	117,324
2010	120,660
2011 -2013	<u>349,488</u>
Future operating lease commitments	<u>\$ 896,601</u>

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Capital Leases

The Department has entered into lease agreements as lessee for financing the acquisition of various vehicles and equipment. These lease agreements qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of their future minimum lease payments as of the inception date. The assets acquired through capital leases are as follows:

	<u>Governmental Activities</u>
Assets:	
Machinery and equipment	\$ 6,122,138
Less accumulated depreciation	<178,671>
Total	<u>\$ 5,943,467</u>

The future minimum lease obligations and the net present value of these minimums lease payments as of June 30, 2005, were as follows:

Year Ending June 30	<u>Governmental Activities</u>
2006	\$ 1,233,944
2007	1,334,501
2008	1,334,501
2009	1,334,501
2010 & Beyond	<u>1,193,854</u>
Total minimum lease payments	6,431,300
Less amount representing interest	<u><521,471></u>
Present value of minimum lease payments	<u>\$ 5,909,829</u>

G. Non-Current Liabilities

Arizona Transportation Board Highway Revenue Bonds

The Transportation Board issued Senior and Subordinated Highway Revenue Bonds to provide funds for acquisition of right-of-way and construction of federal, state and local highways. The original amount of Highway Revenue Bonds issued in prior years and outstanding at the start of the fiscal year was \$1,017,360,000. During the year, Highway Revenue Bonds totaling \$188,260,000 were issued to (i) finance portions of the Transportation Board's Five-Year Transportation Facilities Construction Program, (ii) pay interest on any bonds issued for highway purposes, and (iii) pay costs of issuing the bonds.

The Highway Revenue Bonds are secured by a prior lien on and a pledge of motor vehicle and related fuel fees and taxes of the General Fund (State Highway Fund). Arizona Revised Statutes prohibit the total principal amount of Arizona Highway Revenue Bonds that may be outstanding at any time, excluding refunded bonds, from exceeding \$1.3 billion. Highway Revenue Bonds currently outstanding are as follows:

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Purpose	Interest Rates	Amount
Governmental activities	2.8% - 8.0%	\$ 837,160,000
Governmental activities - refunding	2.75% - 6.0%	324,195,000
		<u>\$1,161,355,000</u>

Annual debt service requirements to maturity for Highway Revenue Bonds are as follows:

Fiscal year ending	Highway Revenue Bonds	
June 30	Principal	Interest
2006	\$ 54,830,000	\$59,749,812
2007	57,825,000	56,805,968
2008	60,645,000	54,040,194
2009	64,190,000	50,696,052
2010	68,140,000	47,493,152
2011-2015	321,265,000	185,314,598
2016-2020	360,675,000	99,887,930
2021-2024	<u>173,785,000</u>	<u>18,090,814</u>
	<u>\$1,161,355,000</u>	<u>\$572,078,520</u>

Arizona Transportation Board Transportation Excise Tax Revenue Bonds

The Maricopa County Regional Area Road Bond Fund is used to record all payments of principal and interest for Transportation Excise Tax Revenue Bonds issued by the Transportation Board. These bonds are secured by transportation excise taxes collected by the Arizona Department of Revenue on behalf of Maricopa County. The original amount of Transportation Excise Tax Revenue Bonds issued in prior years and outstanding at the start of the fiscal year was \$289,000,000.

The Bond Resolution adopted by the Transportation Board on July 25, 1986, established a debt service reserve requirement equal to the maximum annual interest due in the current year or future years on any series of outstanding Transportation Excise Tax Revenue Bonds. The Second Supplemental Transportation Excise Tax Revenue Bond Resolution adopted by the Transportation Board on September 22, 1988, gives the Transportation Board the option, which it has elected, of acquiring debt service reserve insurance policies in lieu of the debt service reserve requirement. Accordingly, no debt service reserve is reflected in the accompanying financial statements. The policies (aggregating \$70,063,698 at June 30, 2005) were issued by Financial Guaranty Insurance Company, except for the 1993 Series Subordinated Bonds policies, which were issued by MBIA Insurance Corporation, and the 1995 Series A and Series B Subordinated Bonds policies which were issued by AMBAC Assurance Corporation. These policies are noncancelable and insure payment, up to the policy amount, of the bond interest on their respective payment dates. The policies shall terminate on the earlier of July 1, 2005, or the date when no respective bonds are outstanding under the Bond Resolution. The premiums on these insurance policies were recorded as expenditures in the year of payment.

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All Transportation Excise Tax Revenue Bonds mature no later than December 15, 2005. Transportation Excise Tax Revenue Bonds currently outstanding are as follow:

Purpose	Interest Rates	Amount
Governmental activities	3.0% - 5.0%	\$ 80,375,000

Annual debt service requirements to maturity for Transportation Excise Tax Revenue Bonds are as follows:

Fiscal year ending	Transportation Excise Tax Revenue Bonds	
June 30	Principal	Interest
2006	\$ 80,375,000	\$ 1,566,542

Arizona Transportation Board Grant Anticipation Notes

The Grant Anticipation Notes Fund administers all payments of principal and interest for notes issued by the Transportation Board and is secured by revenues received from the Federal Highway Administration under grant agreements and certain other federal-aid revenues. The original amount of Grant Anticipation Notes issued in prior years and outstanding at the start of the fiscal year was \$308,585,000. During the year, Grant Anticipation Notes totaling \$104,385,000 were issued to (i) pay costs of the projects (as specified), (ii) pay interest on the notes, and (iii) pay costs of issuing the notes.

Grant Anticipation Notes currently outstanding are as follows:

Purpose	Interest Rates	Amount
Governmental activities	3.0% - 5.25%	\$ 363,970,000

Annual debt service requirements to maturity for Grant Anticipation Notes are as follows:

Fiscal year ending	Grant Anticipation Notes	
June 30	Principal	Interest
2006	\$ 38,540,000	\$ 16,479,893
2007	42,570,000	14,578,218
2008	36,565,000	13,299,868
2009	29,990,000	11,831,556
2010	31,350,000	10,467,556
2011-2015	172,865,000	28,504,964
2016	12,090,000	604,500
	<u>\$363,970,000</u>	<u>\$95,766,555</u>

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Notes Payable

The Department's outstanding notes payable as of June 30, 2005, was \$315,927,190. The governmental activities notes payable was \$169,472,724 and business-type activities was \$146,454,466. The notes payable represent the General Fund (State Highway Fund) loan payable to HELP for \$106,515,135 and the Board Funding Obligations (BFO) for loans from the State Treasurer for \$209,412,055 (principal of \$200,000,000 and accrued interest of \$9,412,055).

Annual debt service requirements to maturity for notes payable are as follows:

Fiscal year ending	Governmental Activities		Business-type Activities	
	Principal	Interest	Principal	Interest
June 30				
2006	\$ 6,515,135	\$ 6,853,270	\$ -	\$ -
2007	30,000,000	2,335,975	-	-
2008	90,000,000	7,599,000	140,000,000	16,160,000
2009	40,000,000	412,875	-	-
	<u>\$166,515,135</u>	<u>\$ 17,201,120</u>	<u>\$140,000,000</u>	<u>\$ 16,160,000</u>

The notes payable amount for governmental activities of \$169,472,724 includes the accrued interest on the BFO of \$2,957,589. The notes payable for business-type activities of \$146,454,466 includes the accrued interest on the BFO of \$6,454,466.

Refunded Bonds Deposited with Escrow Agents

In prior fiscal years, the Transportation Board had refinanced various bond issues through refunding arrangements. Under the terms of the refunding bond issues, sufficient assets to pay all principal, redemption premium, if any, and interest on the refunded bond issues have been placed in irrevocable trust accounts at commercial banks and invested in U.S. Government securities which, together with interest earned thereon, will provide amounts sufficient for future payment of principal and interest of the issues refunded. The assets, liabilities, and financial transactions of these trust accounts and the liability for the defeased bonds are not reflected in the financial statements of the Department.

Refunded bonds of the Department deposited with escrow agents at June 30, 2005, are as follows:

Original Issue	Type	Escrow Maturity Date	Balance
1999 Senior	Highway Refunding Bonds	July 1, 2009	\$ 64,130,000
1998 Series A Senior	Transportation Excise Tax Revenue Bonds	July 1, 2005	1,425,000
1988 Series A	Transportation Excise Tax Revenue Bonds		
	Capital Appreciation Bonds	July 1, 2005	<u>8,996,156</u>
	Total refunded bonds deposited with escrow agents		<u>\$ 74,551,156</u>

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Notes to the Financial Statements
June 30, 2005

Changes in non-current liabilities

The activity for the fiscal year ended June 30, 2005, was as follows:

	Beginning Balance July 1, 2004	Additions	Reductions	Ending Balance June 30, 2005	Due Within One Year
Governmental Activities:					
Bonds and Notes:					
Highway Revenue Bonds	\$ 1,017,360,000	\$ 188,260,000	\$ <44,265,000>	\$ 1,161,355,000	\$ 54,830,000
Transportation Excise Tax					
Tax Revenue Bonds	289,000,000	-	<208,625,000>	80,375,000	80,375,000
Grant Anticipation Notes	308,585,000	104,385,000	<49,000,000>	363,970,000	38,540,000
Premium on Bonds	60,480,591	24,414,008	<8,173,119>	76,721,480	7,024,870
Total bonds and notes	1,675,425,591	317,059,008	<310,063,119>	1,682,421,480	180,769,870
Capital leases	1,120,965	6,434,004	<1,645,140>	5,909,829	1,233,944
Compensated absences	11,023,013	11,589,056	<10,885,432>	11,726,637	9,626,841
Notes payable	165,304,967	48,987,545	<44,819,788>	169,472,724	6,515,135
Total governmental activities	1,852,874,536	384,069,613	<367,413,479>	1,869,530,670	198,145,790
Business-type Activities:					
Compensated absences	151,215	145,537	<163,230>	133,522	133,522
Notes payable	142,414,466	4,040,000	-	146,454,466	-
Total business-type activities	142,565,681	4,185,537	<163,230>	146,587,988	133,522
Total non-current liabilities	<u>\$ 1,995,440,217</u>	<u>\$ 388,255,150</u>	<u>\$ <367,576,709></u>	<u>\$ 2,016,118,658</u>	<u>\$ 198,279,312</u>

Internal service funds predominantly serve the governmental funds. Accordingly, long-term liabilities for them are included as part of the above totals for governmental activities. At year-end, \$569,193 of internal service funds compensated absences and \$5,909,829 of capital leases are included in the above amounts.

Bonds and notes issued by the Department require compliance with a number of covenants. The Department believes that it is in compliance with all such covenants. In addition, certain of the Department's obligations are subject to Internal Revenue Service regulations pertaining to issuance of tax-exempt debt by governmental entities. The Department has not accrued a liability under these regulations.

H. Short-term Debt

The Department had no short-term debt activity for the fiscal year ended June 30, 2005.

I. Fund Balances

Reservations

Effective July 1, 1981, State law required accumulation of at least 15 percent, which in fiscal year 1996 was modified to 12.6 percent, of the revenues allocated each year to the General Fund from the Highway User Revenue Fund for the design, purchase of right-of-way or construction of controlled-access highways which are included in the regional transportation plan of counties with populations in excess of 400,000 (Maricopa and Pima counties). At June 30, 2005, approximately \$134.5 million was reserved in the General Fund (State Highway Fund) for this purpose. The remaining \$6.7 million was restricted for highway construction from Federal highway fatality monies and right of way. The advance from the General Fund (State Highway Fund) for \$20.0 million is reserved for the receivable from the Highway Expansion and Extension Loan Program Fund.

Arizona Department of Transportation
Notes to the Financial Statements
June 30, 2005

The Maricopa Regional Area Road Construction Fund is reserved for capital projects. Capital Projects Fund is reserved for capital projects based on the debt covenants. The Debt Service Fund reserve is for future debt service payments.

6. OTHER INFORMATION

A. Subsequent Events

On July 19, 2005, the Transportation Board issued \$147,400,000 in Highway Revenue Refunding Bonds, Series 2005A to (i) refund portions of the Board's outstanding senior bonds and (ii) pay costs of issuing the Series 2005A Refunding Bonds. The 2005A Bonds are due July 1, 2011, through July 1, 2022. Net proceeds totaled \$161,783,280 (after receipt of \$14,956,636 reoffering premium and payment of \$573,356 in underwriting fees and costs of issuance).

B. Contingent Liabilities

Risk Management Insurance Losses

The Department is exposed to various risks of loss related to torts; thefts of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Department is a participant in the state's self-insurance program, and, in the opinion of the Department's management, any unfavorable outcomes from these claims and actions would be covered by the self-insurance program. Accordingly, the Department has no risk of loss beyond adjustments to future years' premium payments to the state's self-insurance program. All estimated losses for unsettled claims and actions of the state are determined on an actuarial basis and are included in the State of Arizona's Comprehensive Annual Financial Report.

Claims

The Department has a variety of claims pending against it that arose during the normal course of its activities. Management of the Department believes, based on the advice of legal counsel, that losses, if any, resulting from settlement of these claims will not have a material effect on the financial position of the Department.

Grants

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures which may be disallowed by the grantor cannot be determined at this time although the Department expects such amounts, if any, to be immaterial.

Light Rail Transit System

ARS 28-9201 requires the Department to establish, implement and enforce minimum safety standards for light rail transit systems. If a violation of the safety standards is discovered, the Department shall report the violation in writing to the Federal Transit Administration. Furthermore, the organization that operates a light rail transit system shall include a safety oversight function and pay the Department's costs resulting from administration.

C. Retirement Plan

The Arizona State Retirement System Board administers the Arizona State Retirement Plan (Plan), a cost sharing multi-employer public employee defined benefit plan, for the benefit of Arizona employees and employees of certain other governmental entities. Plan provisions, including death, disability, and retirement benefits, are established by state statute. Substantially all employees of the Department are covered by the Plan.

The Arizona State Retirement System (System) issues a Comprehensive Annual Financial Report that includes financial statements and required supplementary information. The most recent report may be obtained by writing the System, 3300 North Central Avenue, P. O. Box 33910, Phoenix, Arizona 85067-3910 or by calling (602) 240-2000 or (800) 621-3778.

Arizona Revised Statutes provide statutory authority for employee and employer contributions. The employee and employer contribution rate for the year ended June 30, 2005, was computed to be 5.2 percent of covered payroll by an actuarial valuation performed at June 30, 2003. The contribution rate for fiscal year 2004 was 2.71 percent. Contributions for the years ended June 30, 2005, 2004 and 2003 were \$8,990,672, \$8,687,059 and \$4,093,262, respectively, for both the employees and the Department, which were equal to the required contributions for each year.

The Department's total payroll for fiscal year 2005 was \$161.8 million. The Plan is funded through payroll deductions from employees' gross earnings and amounts contributed by the Department. Retirement benefits are obligations of the Plan and not of the Department. The Arizona Revised Statutes provide statutory authority for employee and employer contributions. The contribution requirement for fiscal year 2005 was \$9.0 million by both the employees and the Department.

Required Supplementary Information

(Other than MD&A)

Budgetary Comparison Schedule – General Fund (State Highway Fund)

Notes to Required Supplementary Schedule

Information About Infrastructure Assets Reported Using the Modified Approach

Arizona Department of Transportation
Required Supplementary Information
June 30, 2005

Budgetary Comparison Schedule
General Fund (State Highway Fund)
For the fiscal year ended June 30, 2005

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Positive <Negative>
	Original	Final		
Expenditures appropriated by State legislature in 2005 budget:				
Administration:				
Personal services	\$ 18,119,700	\$ 17,513,100	\$ 17,513,088	\$ 12
Employee related expenditures	6,433,700	5,287,200	5,286,688	512
Other operating expenditures	12,131,500	13,804,500	13,798,874	5,626
Attorney General legal service	<u>2,197,000</u>	<u>2,197,000</u>	<u>2,197,000</u>	<u>-</u>
Total Administration	38,881,900	38,801,800	38,795,650	6,150
Highways:				
Personal services	31,985,500	30,572,332	30,572,330	2
Employee related expenditures	10,319,100	9,083,700	9,082,845	855
Other operating expenditures	21,607,500	24,256,068	24,248,750	7,318
Total Highways	<u>63,912,100</u>	<u>63,912,100</u>	<u>63,903,925</u>	<u>8,175</u>
Highway Construction Administration:				
Personal services	27,299,100	20,823,900	20,823,810	90
Employee related expenditures	9,340,800	7,891,700	7,891,194	506
Other operating expenditures	<u>16,472,700</u>	<u>24,397,000</u>	<u>24,392,558</u>	<u>4,442</u>
Total Highway Construction	53,112,600	53,112,600	53,107,562	5,038
Highway Maintenance:				
Personal services	31,440,000	29,000,000	28,761,080	238,920
Employee related expenditures	13,560,000	11,900,000	11,669,171	230,829
Other operating expenditures	61,112,000	65,212,000	62,468,057	2,743,943
Maintenance carryover	<u>2,670,844</u>	<u>2,670,844</u>	<u>2,670,315</u>	<u>529</u>
Total Highway Maintenance	108,782,844	108,782,844	105,568,623	3,214,221

(continued)

Arizona Department of Transportation
Required Supplementary Information
June 30, 2005

Budgetary Comparison Schedule
General Fund (State Highway Fund)
For the fiscal year ended June 30, 2005

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Positive <Negative>
	Original	Final		
Motor Vehicle:				
Personal services	\$ 47,500,000	\$ 44,312,387	\$ 44,312,356	\$ 31
Employee related expenditures	17,200,000	16,397,400	16,397,177	223
Other operating expenditures	17,415,500	21,405,713	21,372,837	32,876
Fee accounting and revenue management system	156,083	156,083	153,181	2,902
Integrated inventory system	99,244	99,244	99,194	50
Security enhancement	2,343,421	2,343,421	802,686	1,540,735
License plates and tabs	2,295,300	2,295,300	2,291,554	3,746
Public information service	150,000	150,000	150,000	-
Special plates	1,535,569	1,535,569	183,712	1,351,857
MVD electronic certificate of title system	18,341	18,341	-	18,341
MVD one-time trailer fees administration	43,724	43,724	-	43,724
MVD Attorney General legal services	140,200	140,200	140,200	-
Abandoned vehicle administration	748,400	748,400	676,888	71,512
Vehicle registration enforcement	383,300	383,300	378,128	5,172
License plate credit	342,500	342,500	245,181	97,319
Motor carrier towing	148,000	148,000	157,392	<9,392>
Total Motor Vehicle	<u>90,519,582</u>	<u>90,519,582</u>	<u>87,360,486</u>	<u>3,159,096</u>
Air Quality Programs:				
Administration air quality project:				
Personal services	38,500	42,169	42,169	-
Employee related expenditures	16,200	16,200	16,200	-
Other operating expenditures	3,900	231	231	-
Total Air Quality Programs	<u>58,600</u>	<u>58,600</u>	<u>58,600</u>	<u>-</u>
Capital outlay - land, buildings and improvements	6,849,155	6,849,155	3,872,392	2,976,763
Arizona Department of Public Safety transfers	32,288,300	32,680,100	32,680,100	-
Expenditures appropriated by State legislature by carryover of previous year's unexpended budget	<u>39,512</u>	<u>39,512</u>	<u>39,512</u>	<u>-</u>
Total expenditures	<u>\$394,444,593</u>	<u>\$394,756,293</u>	<u>\$385,386,850</u>	<u>\$ 9,369,443</u>

The notes to required supplementary information are an integral part of this statement.

Arizona Department of Transportation
Required Supplementary Information
June 30, 2005

Notes to Required Supplementary Information

1. Budgets and budgetary accounting

Annual budgets for the operating expenditures and capital outlay including land, building and improvements for the General Fund (State Highway Fund) are submitted to the Governor in accordance with state law. The budgets are legally enacted as appropriations after approval by the State legislature and signature by the Governor. The legal level of control for operating expenditures is at the program level and expenditure budgets are appropriated using a lump sum format with special line items. Expenditure details for personal services, employee related expenditures and all other operating expenditures are specifically budgeted within all divisions. In certain divisions, other specific programs are budgeted in addition to these categories. Revenue budgets are developed internally by the Department and are not a part of the appropriation process.

Amendments to the approved appropriations require legislative approval. However, since the Department's appropriation is a lump sum appropriation by program, the allocation of funds between personal services, employee-related expenses, and other operating expenditures is an internal decision for the program manager. Accordingly, transfers between line items such as personal services and other operating expenditures within a particular program may be made by the program manager. Transfers of funds between programs require the approval of the Director of the Department of Administration. Expenditures may not exceed appropriations.

All transfers of funds are reported to the Department's Office of Strategic Planning and Budgeting for monitoring purposes.

Budgets are prepared on the cash basis except that liabilities incurred before the end of the fiscal year and paid within the first month of the subsequent fiscal year are charged against the prior fiscal year's budget. The Department's appropriations lapse at year-end unless exempted by the legislature.

For financial reporting purposes, the accompanying financial statements present the legally adopted budget for the operations of the General Fund that is subject to legislative appropriation.

The capital outlay appropriation includes state highway construction and land, buildings and improvements for the General Fund (State Highway Fund). A legal limitation is adopted for land, buildings and improvements; however, legislation allows the Department to spend in excess of its appropriation for state highway construction up to the current fund balance. The Department monitors expenditures through an internal budgetary process and the Five-Year Transportation Facilities Construction Program approved by the Transportation Board.

2. Explanation of difference between budgetary outflows and GAAP expenditures

Actual amounts from the Budgetary Comparison Schedule	\$ 385,386,850
Net increase <decrease> in accounts payable, accrued payroll and other accruals not recognized as expenditures for budgetary basis	990,641
Expenditures which are on the modified accrual basis and not recognized on budgetary basis:	
Capital outlay	243,292,097
Non-capital, including asset preservation	178,512,763
Distribution to other state agencies	2,013,390
Interest expense on loans borrowed from the Highway Expansion and Extension Loan Program	<u>2,514,145</u>
Total expenditures as reported on the Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds (General Fund) - Exhibit 4	<u>\$ 812,709,886</u>

Information About Infrastructure Assets Reported Using the Modified Approach

As allowed by Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments* (GASB 34), the Arizona Department of Transportation (Department) reports its roads and bridges using the modified approach. Assets accounted for under the modified approach include 6,816 center lane miles (18,424 travel lane miles) of roads and 4,608 bridges that the Department is responsible to maintain.

In order to utilize the modified approach, the Department is required to:

- Maintain an asset management system that includes an up to date inventory of eligible infrastructure assets
- Perform condition assessments of eligible assets and summarize the results using a measurement scale
- Estimate each year the annual amount to maintain and preserve the assets at the condition level established and disclosed by the Department
- Document that the assets are being preserved approximately at or above the established condition level

As adopted by the Transportation Board on an annual basis, the Five-Year Transportation Facilities Construction Program (Program) contains estimated expenditures for highway system improvements and the preservation of existing roadway and bridges. Both of these factors impact the condition assessment of the roads and bridges as described in the following sections. The Program in effect for fiscal year 2006 and beyond was adopted by the Transportation Board on June 17, 2005.

This Program is a dynamic instrument and adjustments are made to the annual plans based on the needs of the Department to maintain the condition level of the roads and bridges at a level equal to, or greater than, the goals established by the Department. In addition, not only are adjustments made during the life of the Program, circumstances may require that refinements to the individual components of the Program be made during the fiscal year.

In comparing Estimated to Actual Expenditures, significant variances can occur. These variances are primarily due to the methodology used in the preparation of the Program. In this Program, the Estimated Expenditures for the current year is based on “programmed” projects which may or may not be spent in the current year of the Program. “Programmed” expenditures consist of those items that are planned for the future and contracts have not yet been awarded. Furthermore, the Actual Expenditures will include projects that were “programmed” for a prior year’s Estimated Expenditures but which did not occur, or were not completed, in the prior year.

The following information pertains to the condition assessment and maintenance of infrastructure assets and reflects the Department’s success in achieving condition levels that exceed the established levels.

Roads

The mission of the Department’s Pavement Management Section (PMS) is to develop and provide a cost effective pavement rehabilitation construction program that preserves the State’s investment in its highway system and enhances public transportation and safety. The requirements of GASB 34 and the PMS both work toward the same basic goal, the efficient, effective management of the Department’s assets to produce long term benefits while minimizing expenditures.

The PMS has developed performance goals for the condition level of the pavement in the State highway system. These goals require periodic assessment of pavement conditions and the budget level needed to meet that goal. The goal is expressed as a measure called “Serviceability” which can be defined as the ability of a pavement to serve the traveling public (as documented in 1961 after AASHTO Road Test, 1956-1961). Serviceability is based on detailed measurements of objective features of the pavement. Many surveys since the original road test have shown that these measurements closely track the subjective opinion of the traveling public. Most commonly, this number is called Present Serviceability Rating and abbreviated as PSR. PSR is a five-point scale (5 excellent, 0 impassable), similar to the Weaver/AASHTO Scale shown as follows:

Arizona Department of Transportation
Required Supplementary Information
June 30, 2005

Information About Infrastructure Assets Reported Using the Modified Approach - continued

Numerical Rating	PSR	Weaver/AASHTO Scale
5	Excellent	Perfect
4	Good	Very Good
3	Fair	Good
2	Poor	Fair
1	Very Poor	Poor
0	Impassable	Very Poor

The goal of the Department is to maintain a condition level (PSR) rating of 3.23 or better for all roads in the State highway system. Annually, Transportation Material Technicians drive over the system with inertial profiling equipment and measure the roughness of the pavement. This process is continuous throughout the year in order to assess the condition level of all pavement on an annual basis. As of the end of fiscal year 2005, an overall rating of 3.8 was achieved, as shown in the following graph:

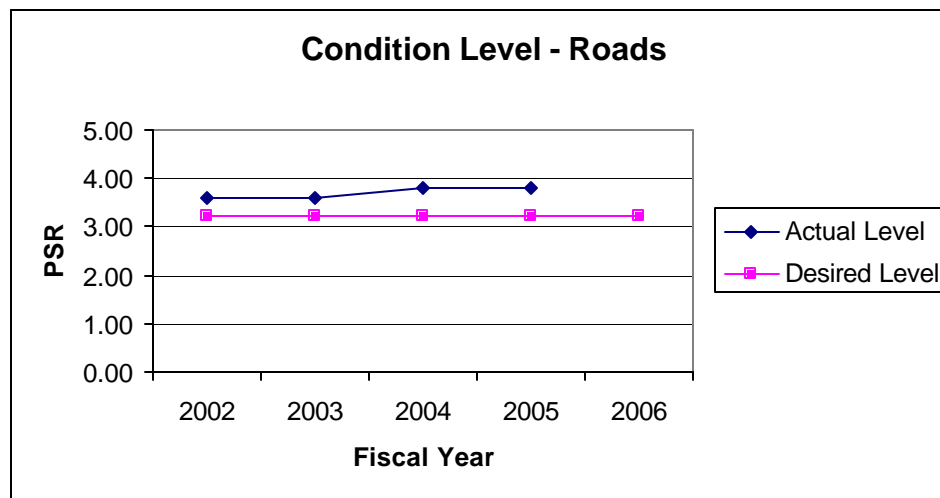


Figure 1

Preservation of the roads is accomplished through programs managed primarily by the ADOT PMS, as well as other units within the Department. The estimated (as specified in the Program as programmed amounts) and actual expenditures for fiscal years 2002 through 2005 were as follows:

Fiscal Year	Estimated Expenditures (in millions)	Actual Expenditures (in millions)
2002	\$227.4	\$234.8
2003	243.5	220.8
2004	198.5	215.5
2005	235.7	196.0

Arizona Department of Transportation
Required Supplementary Information
June 30, 2005

Information About Infrastructure Assets Reported Using the Modified Approach - continued

Bridges

The Department's bridge assets constitute a significant portion of all infrastructure assets in Arizona. As of June 30, 2005, the Department owns and maintains 4,608 bridges with an approximate total deck area of 41,988,500 square feet. Bridges, for purposes of this report, include all structures erected over an opening or depression with a centerline of 20 feet or more. Information related to these bridges is stored and updated in the Arizona Bridge Information and Storage System (ABISS). This system is used to efficiently manage the bridge inventory through storing all bridge related data and assisting bridge engineers in arriving at appropriate bridge preservation decisions. Also, ABISS is used for reporting bridge inventory and condition, on a biennial basis, to the Federal Highway Administration (FHWA).

A Condition Rating Index (CRI) is used to track the condition of the bridge network. The CRI is based on four selected bridge inspection condition ratings, which in turn are based on standards established in the FHWA's "Recording and Coding Guide for the Structural Inventory of the Nation's Bridges". The four selected condition ratings that are included in the CRI computation are: the bridge joints condition, the deck condition, the super-structure condition, and the sub-structure condition. The bridge joints condition rating is an Arizona specific rating item not included in the FHWA condition rating guidelines, whereas the three other condition ratings are federally mandated condition ratings. The CRI is computed by subtracting from one the ratio of the sum of the deck areas of all bridges with a condition rating of four or less (see table below), which indicates that the rated element is at best in a poor condition, to the total sum of the deck areas. The rating system in this guide is as follows:

Numerical Rating	Condition Rating
9	Excellent
8	Very Good
7	Good
6	Satisfactory
5	Fair
4	Poor
3	Serious
2	Critical
1	Imminent Failure

Management of the bridge inventory is a major function of the Department's Bridge Group and regularly scheduled biennial inspections are made of all bridges. A civil or structural engineer, licensed to practice in Arizona, performs these inspections. It is the policy of the Department to maintain State highway bridges so that the CRI exceeds 92.5%. In fiscal year 2005, the CRI was computed at 93.9%.

Information About Infrastructure Assets Reported Using the Modified Approach - continued

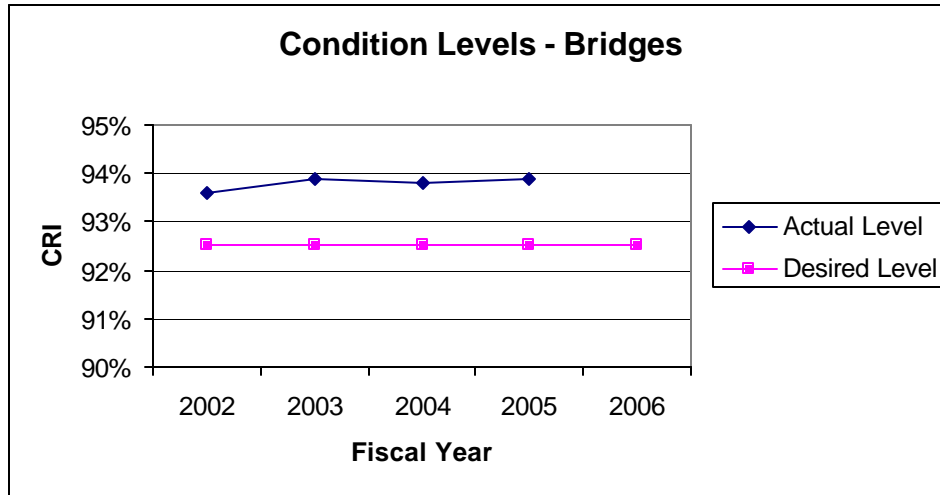
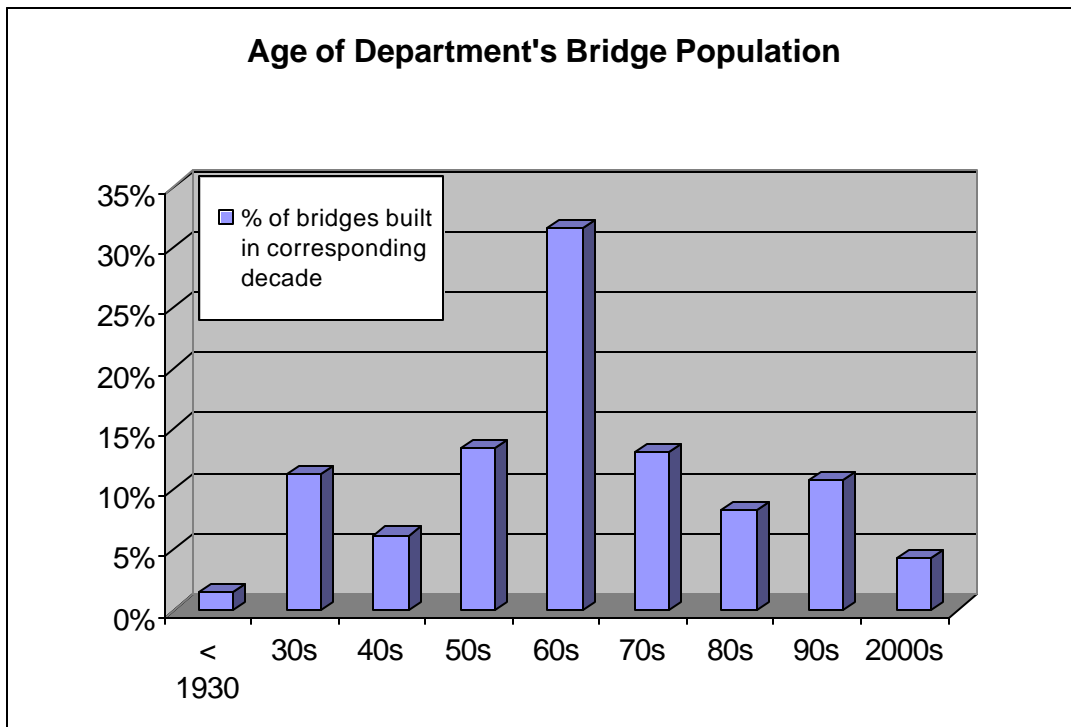


Figure 2

Bridges represent a major public investment and their inspection and maintenance is an essential function of the Department in its mission of products and services for a safe, efficient, and cost effective transportation system. Figure 3 indicates that approximately 64% of the bridges in the state were constructed prior to the 1970s while only 15% have been constructed in the last two decades.



Arizona Department of Transportation
Required Supplementary Information
June 30, 2005

Figure 3

Information About Infrastructure Assets Reported Using the Modified Approach - continued

Preservation of the bridges is accomplished through programs managed by the Bridge Group. The estimated (as specified in the Program as programmed amounts) and actual expenditures for fiscal years 2002 through 2005 were as follows:

Fiscal Year	Estimated Expenditures (in millions)	Actual Expenditures (in millions)
2002	\$14.4	\$18.2
2003	13.6	15.8
2004	12.1	12.2
2005	9.4	10.0

NON-MAJOR GOVERNMENTAL FUNDS FINANCIAL STATEMENTS

SPECIAL REVENUE FUNDS

Special revenue funds are used to account for specific revenues that are legally restricted to expenditures for particular purposes.

The State Aviation Fund is appropriated by the legislature and receives monies from aviation gasoline taxes, sale of abandoned or seized aircraft, flight property taxes and the operation of certain airports. The State Aviation Fund monies are used to build and maintain airport facilities.

The Safety Enforcement and Transportation Infrastructure Fund is appropriated by the legislature and receives monies from the registration of vehicles of nonresidents for enforcement of vehicle safety requirements, maintenance of transportation facilities and upgrades of transportation facilities, including roads, streets, and highways, approved by the Transportation Board within twenty-five miles of the border between Arizona and Mexico.

The Motor Vehicle Liability Insurance Enforcement Fund receives fees and interest to administer the State's Mandatory Liability Insurance Program.

The Vehicle Inspection and Title Enforcement Fund receives monies from continuing appropriation to be used to defray the cost of investigations involving certificates of title, licensing fraud, registration enforcement and other enforcement related issues.

The Motor Carrier Safety Revolving Fund receives fees to administer and enforce the rules governing the safety operations of motor carriers, shippers and vehicles transporting hazardous materials, substances or waste.

The Underground Storage Tank Fund receives certain Motor Vehicle Division revenues for distribution to the Department of Environmental Quality.

The Economic Strength Project Fund collects monies from the Highway User Revenue Fund for use on approved economic strength projects recommended by the Commerce and Economic Development Commission.

The Grant Anticipation Notes Fund receives revenues from the Federal Highway Administration under a grant agreement and certain other federal-aid revenues to accelerate highway construction projects.

The Local Agency Deposits Fund receives monies from the U.S. Government and local agencies for the payment of local agency sponsored county secondary road construction projects.

Arizona Department of Transportation
Combining Balance Sheet
Non-Major Governmental Funds
June 30, 2005

	State Aviation Fund	Safety Enforcement and Transportation Infrastructure Fund	Motor Vehicle Liability Insurance Enforcement Fund	Vehicle Inspection and Title Enforcement Fund	Motor Carrier Safety Revolving Fund
ASSETS					
Unrestricted cash on deposit with the State Treasurer	\$ 20,409,766	\$ 994,903	\$ 8,426,403	\$ 2,551,808	\$ 23,292
Receivables:					
Accrued interest	37,287	2,273	-	-	-
Interfund	77,677	12,347	26,430	13,465	-
Notes and loans	3,969,986	-	-	-	-
Other	297,094	-	-	-	-
Amounts due from:					
U.S. Government	2,215,839	-	-	-	-
Arizona counties and cities	-	-	-	-	-
Restricted cash on deposit with the State Treasurer	-	-	-	-	-
Total assets	<u>\$ 27,007,649</u>	<u>\$ 1,009,523</u>	<u>\$ 8,452,833</u>	<u>\$ 2,565,273</u>	<u>\$ 23,292</u>
LIABILITIES					
Accounts payable	\$ -	\$ -	\$ -	\$ -	\$ -
Accrued payroll and other					
accrued expenditures	60,470	47,577	36,624	33,275	-
Contracts and retainage payable	1,562,845	-	-	-	-
Interfund payables	-	-	-	-	-
Amounts due to:					
Arizona counties and cities	-	-	-	-	-
Other state agencies	-	-	-	-	-
Deferred revenue	3,969,986	-	-	-	-
Total liabilities	<u>5,593,301</u>	<u>47,577</u>	<u>36,624</u>	<u>33,275</u>	<u>-</u>
FUND BALANCES					
Reserved:					
Debt service	-	-	-	-	-
Capital projects	-	-	-	-	-
Unreserved special revenue funds	21,414,348	961,946	8,416,209	2,531,998	23,292
Total fund balances	<u>21,414,348</u>	<u>961,946</u>	<u>8,416,209</u>	<u>2,531,998</u>	<u>23,292</u>
Total liabilities and fund balances	<u>\$ 27,007,649</u>	<u>\$ 1,009,523</u>	<u>\$ 8,452,833</u>	<u>\$ 2,565,273</u>	<u>\$ 23,292</u>

Underground Storage Tank Fund	Economic Strength Project Fund	Grant Anticipation Notes Fund	Local Agency Deposits Fund	Total Non-Major Governmental Funds
\$ -	\$ -	\$ -	\$ -	\$ 32,406,172
5,444	10,799	-	-	55,803
3,142,867	-	-	-	3,272,786
-	-	-	-	3,969,986
-	-	-	1,495,202	1,792,296
-	-	-	5,628,710	7,844,549
-	-	-	40,552	40,552
3,058,066	4,013,723	85	9,817,652	16,889,526
<u>\$ 6,206,377</u>	<u>\$ 4,024,522</u>	<u>\$ 85</u>	<u>\$ 16,982,116</u>	<u>\$ 66,271,670</u>
\$ -	\$ -	\$ -	\$ -	\$ -
-	-	-	-	177,946
-	-	-	5,534,422	7,097,267
-	-	-	-	-
-	4,024,522	-	-	4,024,522
6,206,377	-	-	-	6,206,377
-	-	-	-	3,969,986
<u>6,206,377</u>	<u>4,024,522</u>	<u>-</u>	<u>5,534,422</u>	<u>21,476,098</u>
-	-	85	-	85
-	-	-	11,447,694	11,447,694
-	-	-	-	33,347,793
-	-	85	11,447,694	44,795,572
<u>\$ 6,206,377</u>	<u>\$ 4,024,522</u>	<u>\$ 85</u>	<u>\$ 16,982,116</u>	<u>\$ 66,271,670</u>

Arizona Department of Transportation
Combining Statement of Revenues, Expenditures, and Changes in Fund Balances
Non-Major Governmental Funds
For the fiscal year ended June 30, 2005

	State Aviation Fund	Safety Enforcement and Transportation Infrastructure Fund	Motor Vehicle Liability Insurance Enforcement Fund	Vehicle Inspection and Title Enforcement Fund
Revenues:				
Vehicle registration, title, license and related taxes and fees	\$ 5,322,509	\$ 2,890,062	\$ 2,620,195	\$ 1,642,485
Fuel and motor carrier taxes and fees	488,964	-	-	-
Reimbursement of construction expenditures - federal aid	4,203,044	-	-	-
Reimbursements from Arizona counties and cities		-	-	-
Interest on loans receivable	224,712	-	-	-
Interest on investments	184,560	22,813	-	-
Flight property taxes	13,180,039	-	-	-
Grand Canyon National Park Airport	919,327	-	-	-
Other	546,775	4,166	-	-
Total revenues	<u>25,069,930</u>	<u>2,917,041</u>	<u>2,620,195</u>	<u>1,642,485</u>
Expenditures:				
Current:				
Transportation - appropriated by State legislature:				
Aeronautics	9,516,884	-	-	-
Highway	-	-	-	-
Motor Vehicle	-	1,887,259	950,077	1,002,597
Other	-	-	-	-
Total Transportation - appropriated by State legislature	<u>9,516,884</u>	<u>1,887,259</u>	<u>950,077</u>	<u>1,002,597</u>
Distributions to Arizona counties and cities	4,358,632	-	-	-
Distributions to other state agencies	-	1,226,800	30,000	107,700
Non-capital, including asset preservation	-	176,021	-	-
Total expenditures	<u>13,875,516</u>	<u>3,290,080</u>	<u>980,077</u>	<u>1,110,297</u>
Excess <deficiency> of revenues over <under> expenditures	11,194,414	<373,039>	1,640,118	532,188
Other financing sources <uses>:				
Interfund transfers in	-	-	-	-
Interfund transfers out for debt service	-	-	-	-
Interfund transfers out other	-	<1,896>	-	-
Total other financing sources <uses>	<u>-</u>	<u><1,896></u>	<u>-</u>	<u>-</u>
Net change in fund balances	11,194,414	<374,935>	1,640,118	532,188
Fund balances - July 1	10,219,934	1,336,881	6,776,091	1,999,810
Fund balances - June 30	<u>\$ 21,414,348</u>	<u>\$ 961,946</u>	<u>\$ 8,416,209</u>	<u>\$ 2,531,998</u>

Motor Carrier Safety Revolving Fund	Underground Storage Tank Fund	Economic Strength Project Fund	Grant Anticipation Notes Fund	Local Agency Deposits Fund	Total Non-Major Governmental Funds
\$ 9,667	\$ -	\$ -	\$ -	\$ -	\$ 12,484,918
-	31,803,637	1,000,001	-	-	33,292,602
-	-	-	63,810,417	42,323,474	110,336,935
-	-	-	-	4,760,310	4,760,310
-	-	-	-	-	224,712
-	71,255	101,480	1	-	380,109
-	-	-	-	-	13,180,039
-	-	-	-	-	919,327
-	-	-	-	16,227	567,168
<u>9,667</u>	<u>31,874,892</u>	<u>1,101,481</u>	<u>63,810,418</u>	<u>47,100,011</u>	<u>176,146,120</u>
-	-	-	-	-	9,516,884
-	-	-	-	42,440,134	42,440,134
-	-	-	-	-	3,839,933
-	1,515,929	-	-	-	1,515,929
-	1,515,929	-	-	42,440,134	57,312,880
-	-	1,045,181	-	-	5,403,813
-	30,358,963	56,300	-	-	31,779,763
-	-	-	-	-	176,021
-	31,874,892	1,101,481	-	42,440,134	94,672,477
9,667	-	-	63,810,418	4,659,877	81,473,643
-	-	-	-	26,025	26,025
-	-	-	<63,810,417>	-	<63,810,417>
-	-	-	-	<92,060>	<93,956>
-	-	-	<63,810,417>	<66,035>	<63,878,348>
9,667	-	-	1	4,593,842	17,595,295
13,625	-	-	84	6,853,852	27,200,277
<u>\$ 23,292</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 85</u>	<u>\$ 11,447,694</u>	<u>\$ 44,795,572</u>

FIDUCIARY FUND FINANCIAL STATEMENTS AGENCY FUNDS

Combining Statement of Net Assets

Statement of Changes in Assets and Liabilities

AGENCY FUNDS

Highway Properties - Privilege Tax Fund collects monies from renters of properties previously acquired by the Department for use in future highway development. Monies collected are distributed to the Department of Revenue.

Highway Properties - 24% Lieu Tax Fund collects 24 percent of the Department's rental income from properties for use in future highway development. Monies collected are distributed to the local counties.

Arizona Department of Transportation
Combining Statement of Net Assets
Agency Funds
June 30, 2005

	Highway Properties -Privilege Tax Fund	Highway Properties - 24 % Lieu Tax Fund	Total
ASSETS			
Restricted cash on deposit with the State Treasurer	\$ 220	\$ 248,195	\$ 248,415
Total assets	<u>\$ 220</u>	<u>\$ 248,195</u>	<u>\$ 248,415</u>
LIABILITIES			
Due to Department of Revenue	\$ 220	\$ -	\$ 220
Due to Arizona counties	<u>-</u>	<u>248,195</u>	<u>248,195</u>
Total liabilities	<u>\$ 220</u>	<u>\$ 248,195</u>	<u>\$ 248,415</u>

Arizona Department of Transportation
Statement of Changes in Assets and Liabilities
Agency Funds
For the fiscal year ended June 30, 2005

	Balance July 1, 2004	Additions	Deductions	Balance June 30, 2005
<hr/> Highway Properties - Privilege Tax <hr/>				
ASSETS				
Restricted cash on deposit with the State Treasurer	\$ 195	\$ 3,409	\$ <3,384>	\$ 220
Total assets	<u>\$ 195</u>	<u>\$ 3,409</u>	<u>\$ <3,384></u>	<u>\$ 220</u>
 LIABILITIES				
Due to Department of Revenue	\$ 195	\$ 3,409	\$ <3,384>	\$ 220
Total liabilities	<u>\$ 195</u>	<u>\$ 3,409</u>	<u>\$ <3,384></u>	<u>\$ 220</u>
 <hr/> Highway Properties - 24 % Lieu Tax <hr/>				
ASSETS				
Restricted cash on deposit with the State Treasurer	\$ 223,385	\$ 249,886	\$ <225,076>	\$ 248,195
Total assets	<u>\$ 223,385</u>	<u>\$ 249,886</u>	<u>\$ <225,076></u>	<u>\$ 248,195</u>
 LIABILITIES				
Due to Arizona counties	\$ 223,385	\$ 249,886	\$ <225,076>	\$ 248,195
Total liabilities	<u>\$ 223,385</u>	<u>\$ 249,886</u>	<u>\$ <225,076></u>	<u>\$ 248,195</u>

CAPITAL ASSETS

CAPITAL ASSETS USED IN THE OPERATION OF GOVERNMENTAL FUNDS

Schedule by Source

Schedule by Function and Activity

Schedule of Changes by Function and Activity

Arizona Department of Transportation
Capital Assets Used in the Operation of Governmental Funds
Schedule by Source¹
June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Governmental funds capital assets:		
Land	\$ 1,875,770,486	\$ 1,858,113,828
Buildings and improvements	146,707,482	145,768,717
Improvements other than buildings	34,732,256	34,032,364
Machinery and equipment	46,235,293	43,707,436
Infrastructure	8,863,627,692	8,591,370,633
Construction in progress	<u>1,723,624,210</u>	<u>1,401,933,559</u>
Total governmental funds capital assets	<u>\$ 12,690,697,419</u>	<u>\$ 12,074,926,537</u>
 Investment in governmental funds capital assets by source:		
Government funds	\$ 12,690,697,419	\$ 12,074,926,537
Total governmental funds capital assets	<u>\$ 12,690,697,419</u>	<u>\$ 12,074,926,537</u>

¹ This schedule presents only the capital assets balances related to governmental funds. Accordingly, the capital assets reported in the internal service fund are excluded from the above amounts. Generally, the capital assets of the internal service fund are included as governmental activities in the statement of net assets.

Arizona Department of Transportation
Capital Assets Used in the Operation of Governmental Funds
Schedule By Function and Activity¹
June 30, 2005

Function and Activity	Land	Buildings and Improvements	Improvements other than Buildings	Machinery and Equipment	Infrastructure	Construction in Progress	Total
Administration	\$ 879,017	\$ 14,828,184	\$ 753,950	\$ 9,352,868	\$ -	\$ -	\$ 25,814,019
Aeronautics	-	297,868	19,907,982	1,106,360	-	-	21,312,210
Highway:							
Administrative and other services	935,955	33,875,622	1,646,171	4,678,802	-	-	41,136,550
Highway construction	1,859,226,124	4,648,473	284,610	6,327,542	8,863,627,692	1,723,624,210	12,457,738,651
Highway development	-	-	-	3,281,586	-	-	3,281,586
Materials engineering	-	4,844,126	7,077	3,753,381	-	-	8,604,584
Traffic engineering	-	320,207	21,667	1,350,811	-	-	1,692,685
Transportation planning and research	-	-	122,946	654,196	-	-	777,142
Highway Maintenance	4,907,328	41,490,801	8,436,237	7,015,689	-	-	61,850,055
Motor Vehicle	9,822,062	46,402,201	3,551,616	8,714,058	-	-	68,489,937
Total governmental funds capital assets	\$ 1,875,770,486	\$ 146,707,482	\$ 34,732,256	\$ 46,235,293	\$ 8,863,627,692	\$ 1,723,624,210	\$ 12,690,697,419

¹ This schedule presents only the capital assets balances related to governmental funds. Accordingly, the capital assets reported in the internal service fund are excluded from the above amounts. Generally, the capital assets of the internal service fund are included as governmental activities in the statement of net assets.

STATISTICAL SECTION

Table 1

Arizona Department of Transportation
Government-wide Expenses by Function
For the fiscal year ended June 30
(Thousands of Dollars)

Fiscal				Highway	Motor	Distributions to		Interest on		Arizona	Highway	Expansion	
Year	Administration	Aeronautics	Highway	Maintenance/1	Vehicle	and other State	Inter-	long-term	Other	Highways	Magazine	and	Total
						agencies	governmental	debt				Loan	
												Program	
2005	\$ 42,298	\$ 9,804	\$ 72,665	\$ 314,938	\$ 91,676	\$ 1,393,808	\$ 42,440	\$ 86,870	\$ 6,871	\$ 10,270	\$ 4,360	\$ 2,076,000	
2004	57,703	7,512	48,797	474,430	86,845	1,183,797	39,205	89,431	9,815	10,007	4,414	2,011,956	
2003	52,533	3,848	45,644	374,328	83,090	1,149,593	30,235	84,084	8,460	11,118	26,349	1,869,282	
2002	57,864	3,751	46,543	188,198	82,904	1,064,560	24,791	89,605	6,844	10,711	5,265	1,581,036	

NOTE: Implemented GASB 34 in fiscal year 2002. Therefore, government-wide financial information for years prior to fiscal year 2002 is not available.

/1 Includes Non-capital, including asset preservation

Table 2

Arizona Department of Transportation
Government-wide Revenues
For the fiscal year ended June 30
(Thousands of Dollars)

Fiscal Year	Program Revenues			General Revenues			Total
	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Taxes	Other Revenues	Interest on Investments	
2005	\$ 126,267	\$ 58,948	\$ 484,276	\$ 2,056,503	\$ 27,120	\$ 19,245	\$ 2,772,359
2004	131,025	44,008	418,174	1,907,984	25,279	9,940	2,536,410
2003	130,889	34,160	453,758	1,798,243	21,729	22,243	2,461,022
2002	124,565	56,481	470,772	1,720,030	27,148	35,488	2,434,484

NOTE: Implemented GASB 34 in fiscal year 2002. Therefore, government-wide financial information for years prior to fiscal year 2002 is not available.

Table 3

Arizona Department of Transportation
General Governmental Expenditures by Functions/Programs
Last Ten Fiscal Years
For the fiscal year ended June 30
(Thousands of Dollars)

Fiscal Year	Administration/1	Aeronautics	Highway/2	Highway Maintenance	Motor Vehicle	Distributions to Arizona counties, cities and other State agencies/3	Debt Service	Capital Outlay and Non-capital, including asset preservation/4	Other/5	Total
2005	\$ 40,599	\$ 9,517	\$ 106,184	\$ 105,887	\$ 90,208	\$ 1,393,808	\$ 394,032	\$ 833,730	\$ 6,312	\$ 2,980,277
2004	56,484	7,228	85,258	95,144	84,921	1,182,797	374,352	978,607	8,319	2,873,110
2003	51,485	3,579	74,244	94,978	81,518	1,146,840	330,203	989,494	7,507	2,779,848
2002	56,230	3,491	68,369	89,314	81,012	1,038,314	292,979	1,105,917	33,526	2,769,152
2001	48,150	18,280	43,117	89,400	77,337	-	292,930	1,008,590	34,310	1,612,114
2000	47,847	21,640	42,302	83,398	74,492	-	253,823	941,913	43,927	1,509,342
1999	44,648	26,787	42,035	79,304	67,144	-	226,928	853,695	62,600	1,403,141
1998	43,914	30,734	41,381	76,597	63,056	-	199,948	602,955	65,625	1,124,210
1997	43,981	18,975	40,230	70,336	30,147	-	210,446	540,203	84,433	1,038,751
1996	36,406	11,107	111,884	-	33,486	-	200,364	555,087	87,960	1,036,294

NOTES: FY 2002-2005 includes expenditures that were considered Agency Funds in prior years.

/1 Includes the Director's Office, Financial Management (formerly Administrative) Services, Transportation Services Group and the Department's Risk Management Premium.

/2 Includes Transportation Planning for FY 1997-2000.
Includes Highway Maintenance for FY 1996.

/3 FY 2002 includes expenditures that are distributed to General Fund (State Highway Fund), Cities, Counties and other State Agencies.

/4 Named Highway Construction in years prior to FY 2002. For years prior to 1999, includes Expendable Trust Fund.

/5 FY 2002 includes interest on loans payable, State appropriations and DPS distributions - appropriated by State legislature.
FY 2001 includes other and Arizona Department of Public Safety (DPS) distributions - appropriated by State legislature.

Includes Transportation not appropriated, Land, Buildings & Improvements, Leases Payable and Transfers for FY 1997-2000.

Includes Reimbursements, Transfers, Director's Office, Highway Safety Office and Land, Buildings and Improvements for FY 1996.

Arizona Department of Transportation
General Governmental Revenues by Source
Last Ten Fiscal Years
For the fiscal year ended June 30
(Thousands of Dollars)

Fiscal Year	Transportation Excise Taxes/1	Motor Fuel Taxes and Fees/1	Vehicle Reg., Title, License and Related Fees/1	Expenditures of Federal Awards /2	Reimburse- ments	Interest on Investments	Other/3	Total
2005	\$ 316,806	\$ 759,633	\$ 1,080,391	\$ 512,724	\$ 34,535	\$ 19,162	\$41,248	\$ 2,764,499
2004	288,600	712,040	1,009,370	427,366	38,945	8,333	33,328	2,517,982
2003	268,721	695,503	935,389	466,354	26,102	19,702	25,191	2,436,962
2002	267,563	658,535	892,093	522,036	12,664	29,697	34,405	2,416,993
2001	-	300,750	219,746	428,290	17,150	44,648	292,416	1,303,000
2000	-	276,189	255,088	414,015	18,788	41,534	267,004	1,272,618
1999	-	298,394	250,121	401,464	15,748	34,377	257,479	1,257,583
1998	-	273,806	210,370	283,982	8,505	34,382	223,486	1,034,531
1997	-	288,878	198,002	305,438	15,083	33,238	231,792	1,072,431
1996	-	291,000	171,823	268,605	32,711	29,603	228,698	1,022,440

NOTES: /1 FY 2002-2005 includes revenues that were considered Agency Funds in prior years.

/2 For years prior to 1999, includes Expendable Trust Fund.

/3 Includes interest on loans receivable, flight property taxes, Grand Canyon National Airport, and other.

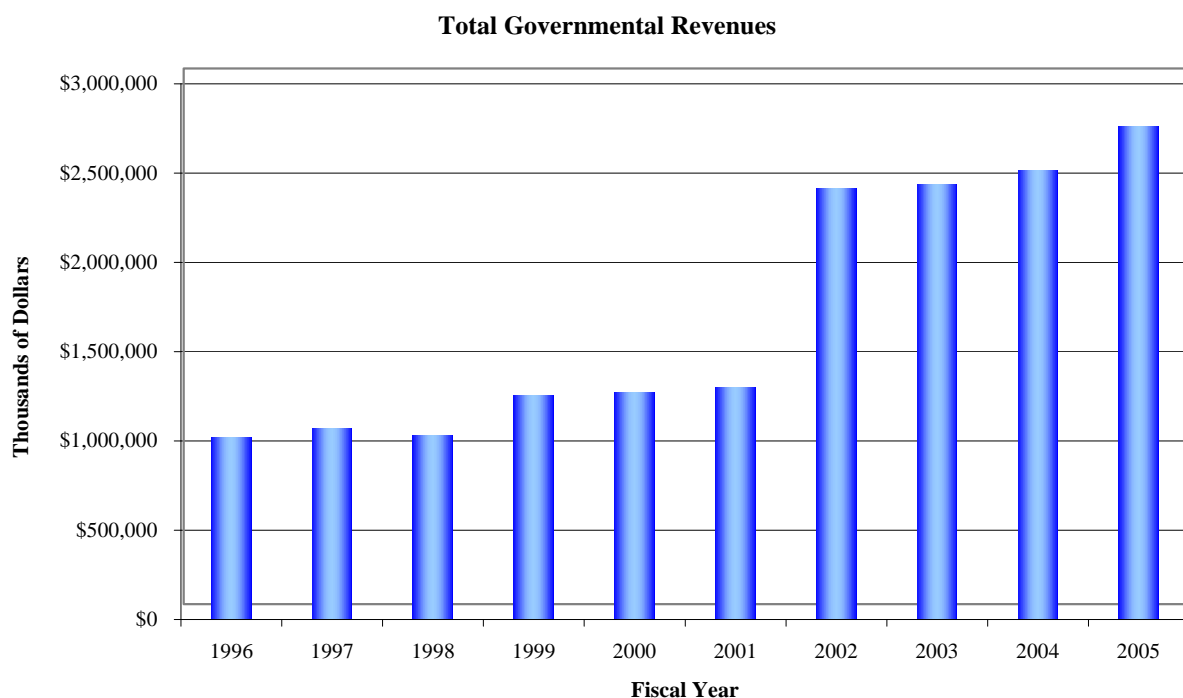


Table 5

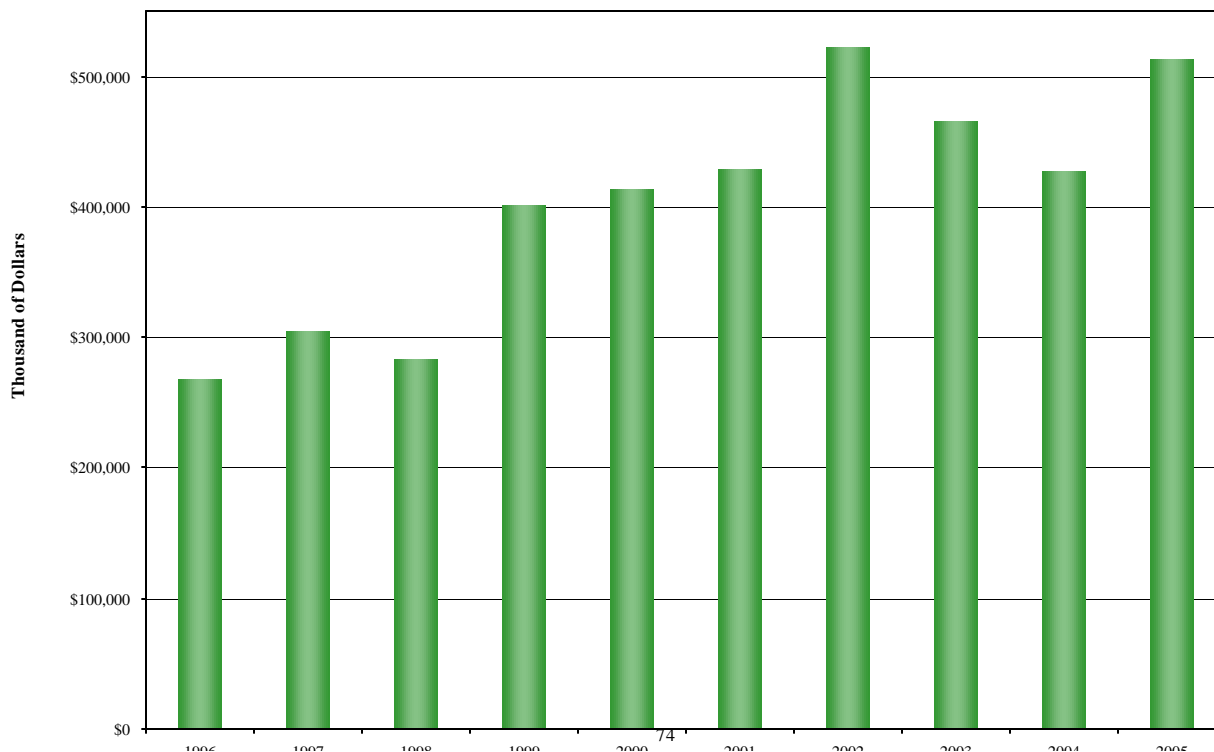
Arizona Department of Transportation
Expenditures of Federal Awards /1
For the fiscal year ended June 30
(Thousands of Dollars)

Fiscal Year	FAA	FRA	FTA	NHTSA	FHWA	FMCSA	BLM	BIA	Sub-total	FHWA /2	Total
2005	\$ 4,203	\$ -	\$ 8,466	\$ 96	\$456,924	\$ 282	\$ 152	\$ 278	\$470,401	#####	#####
2004	480	-	5,549	84	384,416	434	79	-	391,042	36,324	427,366
2003	242	-	6,618	87	433,472	466	30	-	440,915	25,439	466,354
2002	-	3	5,264	83	496,509	282	47	-	502,188	19,848	522,036
2001	-	14	4,746	65	390,204	-	-	-	395,029	33,261	428,290
2000	6	2	3,717	65	393,958	-	-	1,048	398,796	15,219	414,015
1999	6,278	69	5,107	275	371,013	-	-	974	383,716	17,748	401,464
1998	2,379	14	3,392	49	278,148	-	-	-	283,982	-	283,982
1997	91	130	2,508	-	302,633	-	-	76	305,438	-	305,438
1996	506	499	3,552	-	261,820	-	-	2,228	268,605	-	268,605

SOURCE: Single Audit Reports - fiscal years 1996 through 2005.

NOTES: /1 Federal Aviation Administration (FAA); Federal Railroad Administration (FRA);
Federal Transit Administration (FTA) - previously Urban Mass Transit Administration
(UMTA); National Highway Transportation Safety Administration (NHTSA); Federal
Highway Administration (FHWA); Federal Motor Carrier Safety Administration (FMCSA);
Bureau of Land Management (BLM); Bureau of Indian Affairs (BIA);
and Department of Agriculture (DOA).
/2 Prior to 1999, the Local Agency Deposits Fund was an Expendable Trust
Fund. It is now a Special Revenue Fund.

Total Expenditures of Federal Awards



Arizona Department of Transportation
 Fuel Tax Rates
 For the fiscal year ended June 30
 (Cents per Gallon)

<u>Fiscal Year</u>	<u>Effective Date</u>	<u>Gasoline Tax</u>	<u>Use Fuel Tax /1</u>
2005	-	18	26
2004	-	18	26
2003	-	18	26
2002	-	18	26
2001	7/1/2000	18	26
2000	-	18	27
1999	-	18	27
1998	12/31/1997	18	27
1997	-	18	18
1996	-	18	18

SOURCE: Arizona Revised Statutes §28-5606

NOTE: Gasohol is currently taxed at the same rate as gasoline
 and use fuel. Use fuel is primarily diesel fuel.

/1 Lightweight motor vehicles under 26,000 pounds pay \$.18 per gallon.

Table 7

Arizona Department of Transportation
Highway User Revenue Fund Collections
For the fiscal year ended June 30
(Thousands of Dollars)

Fiscal Year	Motor Veh. Fuel Tax Revenue	Motor Veh. Reg. Fee Revenues	Motor Carrier Tax Revenues	Motor Veh. Operators' License Fees and Other Fees	Motor Veh. License (In Lieu) Tax Revenues	Total Deposited To Arizona Hwy. User Rev. Fund
2005	\$ 701,965	\$ 163,463	\$ 18,573	\$ 50,789	\$ 318,689	\$ 1,253,479
2004	656,881	163,689	16,623	42,829	309,688	1,189,710
2003	633,826	158,726	23,302	39,906	276,279	1,132,039
2002	629,360	151,437	11,896	40,122	259,308	1,092,123
2001	566,115	148,336	15,094	43,248	251,496	1,024,289
2000	545,901	158,424	15,040	43,508	235,287	998,160
1999	636,117	145,340	14,409	15,939	217,905	1,029,710
1998	508,544	109,445	56,123	36,426	176,950	887,488
1997	488,701	101,528	90,186	41,294	175,253	896,962
1996	473,741	97,601	85,433	42,654	160,145	859,574

SOURCES: Basic Financial Statements - Fiscal Years 2002 through 2005, General Purpose Financial Statements - Fiscal Years 1996 through 2001, Arizona Highway User Revenue Fund Revenue Collections by Category - Fiscal Years 1996 through 1998.

Highway User Revenue Fund Collections

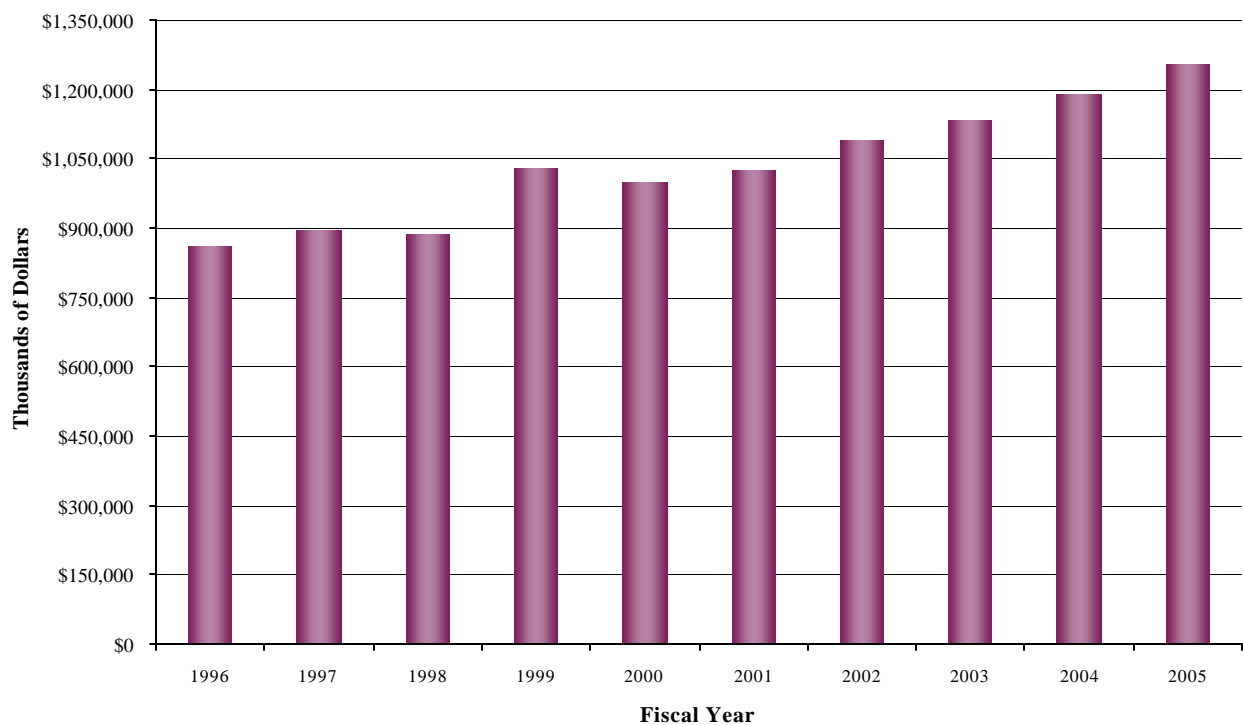


Table 8

Arizona Department of Transportation
 Highway User Revenue Fund Distributions
 For the fiscal year ended June 30
 (Thousands of Dollars)

Fiscal Year	State Highway Fund	Cities and Towns	Counties	Department of Public Safety	Economic Strength Project Fund	Other /1	Total
2005	\$ 483,047	\$ 362,965	\$ 226,110	\$ 52,216	\$ 1,000	\$128,141	\$ 1,253,479
2004	570,801	344,699	214,731	48,698	1,000	9,781	1,189,710
2003	537,668	324,431	202,105	54,416	1,000	12,419	1,132,039
2002	519,837	312,252	195,530	37,066	1,000	26,438	1,092,123
2001	503,611	305,009	188,982	10,937	1,000	14,750	1,024,289
2000	493,697	323,798	157,594	13,622	1,000	8,449	998,160
1999	512,149	295,879	199,591	12,630	1,000	8,461	1,029,710
1998	435,882	263,220	163,973	14,688	1,000	8,519	887,282
1997	444,927	268,696	167,350	17,188	1,000	9,289	908,450
1996	429,171	256,901	152,571	19,688	1,000	9,304	868,635

The Highway User Revenue Fund receives certain Motor Vehicle Division revenues from the Motor Vehicle Division Clearing Fund. These monies are distributed to the State Highway Fund and various counties and cities, based on statutory formulas.

SOURCES: Basic Financial Statements - Fiscal Years 2002 through 2005, General Purpose Financial Statements - Fiscal Years 1996 through 2001, Monthly Reports MV675580-01 fiscal years 1996 through 2005 (adjusted for accrual basis).

NOTES: /1 In fiscal years 1996 through 2005, an appropriation for Arizona State Parks is included. Fiscal years 2002 and 2005 include distributions to State General Fund.

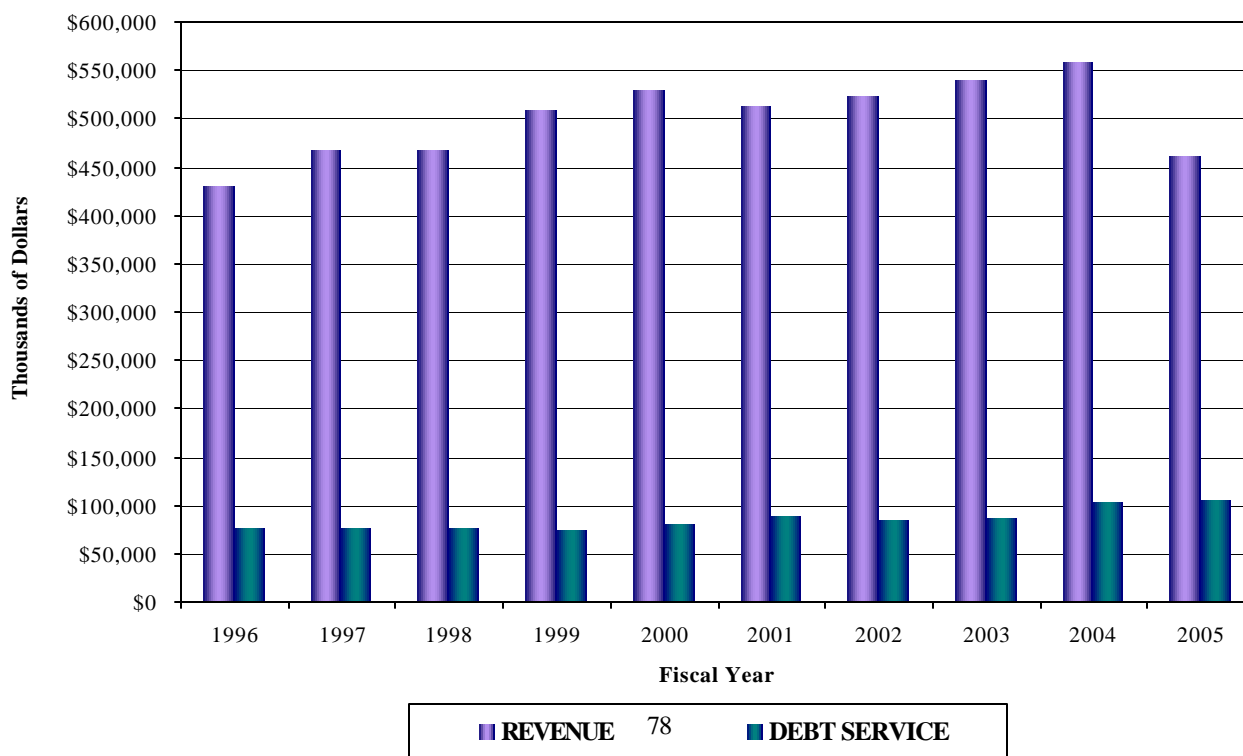
Arizona Department of Transportation
Bond Coverage
Highway User Revenue Fund Series
For the fiscal year ended June 30
(Thousands of Dollars)

Fiscal Year	Principal	Interest	Total	Pledged Revenues /1	Coverage
2005	\$ 44,265	\$ 60,459	\$ 104,724	\$ 461,763	4.4
2004	51,155	53,149	104,304	557,854	5.3
2003	44,490	41,932	86,422	540,540	6.3
2002	45,365	38,534	83,899	523,326	6.2
2001	52,055	36,581	88,636	513,890	5.8
2000	46,270	33,994	80,264	528,721	6.6
1999	43,805	31,090	74,895	509,935	6.8
1998	43,405	33,266	76,671	468,240	6.1
1997	40,970	36,148	77,118	468,542	6.1
1996	38,430	38,770	77,200	429,825	5.6

SOURCES: Highway User Revenue Fund Schedule 1 Summary For Revenue Collected
Monthly Reports MV675577-1 fiscal years 1996 through 2005;
Debt Service Funds - fiscal years 1996 through 2005.

/1 For fiscal year 1996, net of 7% distributed to cities with a population greater than 300,000 persons. For fiscal years 1997 and after, includes vehicle license tax revenues distributed directly to the State Highway Fund.
Fiscal year 2005 is net of a \$118 million distribution to the State General Fund.

Highway User Revenue Fund Series Bond Coverage



Arizona Department of Transportation
Legal Debt Margin
Highway User Revenue Fund
For the fiscal year ended June 30
(Thousands of Dollars)

Fiscal Year	Debt Limit/1	Total Principal Applicable to Limit	Legal Debt Margin	Total Principal Applicable to the Limit as a Percentage of Debt
				Limit
2005	\$1,300,000	\$1,161,355	\$138,645	89.34%
2004	1,300,000	1,017,360	282,640	78.26%
2003	1,300,000	932,700	367,300	71.75%
2002	1,000,000	734,155	265,845	73.42%
2001	800,000	700,280	99,720	87.54%
2000	800,000	608,500	191,500	76.06%
1999	800,000	524,345	275,655	65.54%
1998	800,000	568,150	231,850	71.02%
1997	800,000	611,555	188,445	76.44%
1996	800,000	652,525	147,475	81.57%

NOTE: /1 The statutory limitation on the issuance of bonds, as outlined in ARS §28-7510, applies only to the Highway User Revenue Fund (HURF). The only limitation on Maricopa County Regional Area Road Fund (RARF) and Grant Anticipation Notes (GANS) is the ability to secure the debts with available excise tax monies and available grant revenues, respectively.

Arizona Department of Transportation
Bond Coverage
Regional Area Road Fund Series
For the fiscal year ended June 30
(Thousands of Dollars)

Fiscal Year	Principal	Interest	Total	Revenues	Coverage
2005	\$208,625	\$14,318	\$ 222,943	\$ 316,806	1.4
2004	199,400	23,553	222,953	288,600	1.3
2003	190,415	31,533	221,948	268,721	1.2
2002	163,455	35,445	198,900	267,563	1.3
2001	156,865	40,035	196,900	264,722	1.3
2000	128,805	42,609	171,414	248,596	1.5
1999	106,765	43,251	150,016	229,470	1.5
1998	82,765	40,512	123,277	209,263	1.7
1997	78,015	45,248	123,263	192,257	1.6
1996	76,955	46,209	123,164	178,413	1.4

SOURCE: Maricopa County Regional Area Road Fund Report.

NOTE: Bond coverage ratio is based upon total Maricopa County Transportation Excise Tax collections.

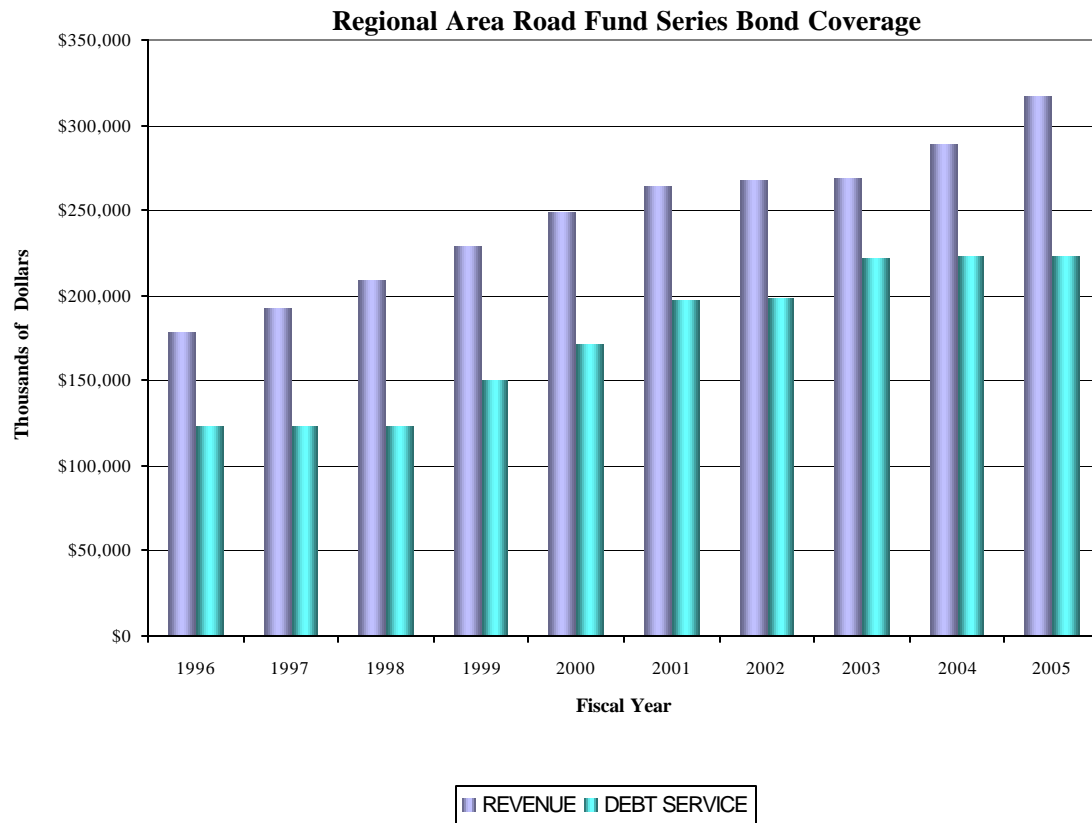


Table 12

Arizona Department of Transportation
 Total Public Road Mileage By Highway Class and Governmental Ownership
 For the calendar year ended December 31, 2004
 (With comparative totals for the calendar year ended December 31, 2003)
 (In Center Lane Miles)

<u>FUNCTIONAL CLASSIFICATION</u>	<u>STATE</u>	<u>COUNTY</u>	<u>MUNICIPAL</u>	<u>FEDERAL</u>	<u>TOTAL</u>	
					<u>2004</u>	<u>2003</u>
RURAL:						
Interstate Freeway	980	-	-	-	980	980
Principal Arterial	1147	20	18	2	1,187	1,141
Minor Arterial	1169	142	29	3	1,343	1,276
Major Collector	1758	1,548	265	730	4,301	4,233
Minor Collector	413	1,073	131	593	2,210	2,117
Local	411	13,948	1,632	10,025	26,016	26,004
TOTAL RURAL	<u>5,878</u>	<u>16,731</u>	<u>2,075</u>	<u>11,353</u>	<u>36,037</u>	<u>35,751</u>
URBAN:						
Interstate Freeway	188	-	-	-	188	187
Urban Expressway	142	1	7	-	150	145
Principal Arterial	302	113	741	-	1,156	1,087
Minor Arterial	93	229	953	4	1,279	1,189
Urban Collector	37	677	1,394	53	2,161	2,200
Local	176	1,747	14,830	389	17,142	16,969
TOTAL URBAN	<u>938</u>	<u>2,767</u>	<u>17,925</u>	<u>446</u>	<u>22,076</u>	<u>21,777</u>
STATEWIDE COMPOSITE:						
Freeways and Expressways	1,310	1	7	-	1,318	1,312
Arterials	2,711	504	1,741	9	4,965	4,693
Collectors	2,208	3,298	1,790	1,376	8,672	8,550
Locals	587	15,695	16,462	10,414	43,158	42,973
TOTAL STATEWIDE	<u>6,816</u>	<u>19,498</u>	<u>20,000</u>	<u>11,799</u>	<u>58,113</u>	<u>57,528</u>

SOURCE: Arizona's Highway Performance Monitoring System (HPMS) 2004 & 2003 Data

ACKNOWLEDGMENTS

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**State of Arizona
Department of Transportation**

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